Tax Reform Hearing on the Benefits of Permanent Tax Policy for America's Job Creators

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Vice President of Tax, Brunswick Corporation

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Tax Reform Hearing on the Benefits of Permanent Tax Policy for America's Job Creators

U.S. House of Representatives,
Committee on Ways and Means,
Washington, D.C.

Advisory

The Committee met, pursuant to notice, at 10:05 a.m. in Room 1100, Longworth House Office Building, Hon. Dave Camp [Chairman of the Committee] presiding.

*Chairman Camp. This hearing will come to order, if everyone will take their seats, please.

Good morning, and welcome to the first Ways and Means Committee hearing on elements of the tax reform discussion draft I released in February.

The draft is focused on two primary goals; making the Tax Code simpler and fairer for families and employers, and strengthening the economy so there are more jobs and bigger paychecks for American families.

As we explore what tax reform means to the American economy and for American families, we must move away from short term tax policy and work toward greater certainty in the Tax Code.

When I released the draft, the first item I asked for public feedback on was the extenders and our revenue baseline.

The question is not only about the merits of the individual policy but how we should treat the revenue gained or lost for either making those policies permanent, reforming them, or repealing them.

Today's hearing will help the Committee find answers to these questions. One thing everyone in this room can agree on is that today's Tax Code is too complex, and one of the best examples of the complexity of our current Tax Code is so-called "tax extenders" and their temporary status.

As such, job creators are left constantly guessing if a group of policies are going to be around next year. Families and employers literally do not know what tax benefits they will be able to take advantage of from year to year, yet when examining some of these provisions, such as the research and development tax credit, we find out that some have been around for 30 years or more.

This is no way to write tax policy, let alone try to run an economy. The United States is the only country in the world that allows such important pieces of the Tax Code to expire on a regular basis.

How can we expect businesses to plan on new hire's or increased wages for workers when they do not know what their operating costs will be from year to year?

Our draft makes permanent seven business tax provisions that expired at the end of 2013. These policies must still be evaluated in the context of pro-growth tax reform and how making those permanent will help grow the economy, simplify the Tax Code, and lower tax rates.

Making some tax policies permanent now will open the door for the economic growth we need by giving consistency and stability to businesses small and large.

Specifically today we will address the research and development tax credit, small business expensing, the active financing exception, depreciation for certain race horses, CFC look-through, and two S corporation provisions.

It is important to note that most of these provisions have had bipartisan support in the past. For example, prior to heading the Committee, Sandy Levin and I sponsored the House bill to extend the research and experimentation tax credit.

The witnesses we have before us today will help ignite an important discussion on the merits of these particular extender policies, specifically how to allow Americans to innovate and create jobs and invest.

By supporting permanent policies, Washington can promote certainty for American businesses and generate additional economic growth.

The Committee's work will not end here. This is just the beginning of the conversation that we must have in order to overhaul the Tax Code so it is simpler and fairer for families.

You have heard from me before and you will continue to hear it, we can no longer accept the status quo. Washington needs to wake up to this reality and start offering concrete solutions and debating real policies that strengthen the economy and help hard working taxpayers, and tax reform is one way we can do that.

I look forward to hearing from our witnesses today and to working with members on both sides of the aisle on legislation we can move forward to address the provisions we discuss today.

At this time I will recognize Mr. Levin for an opening statement.

*Mr. Levin. Thank you, Mr. Chairman. Welcome, all of you. Today's hearing purports to discuss the benefits of permanent tax policy. I think we all agree that permanent tax policy provides certainty for all taxpayers, individuals and businesses, and is preferable to frequent short term extensions.

What is missing from the agenda today is any discussion of how to pay for making tax extenders permanent. The Republican tax reform proposal that was unveiled six weeks ago set forth a business tax reform plan that made these and other temporary provisions permanent, and did not add to the deficit in the first ten years.

In fact, that was pinpointed, even celebrated by some as a hallmark of the proposal. Yet, the concept of fiscal responsibility has now been left behind with today's hearing focused on making seven of the roughly so-called extenders permanent as they were in the Republican tax reform draft, without discussing the provisions that would offset the costs of such action.

We do not agree that adding more than $125 billion to the deficit to make these seven expired tax provisions permanent or provide them with a long term extension is fiscally responsible, and should take priority over discussing the entire package of tax extenders.

Fiscal responsibility cannot simply be a talking point that is set aside when it comes to providing tax incentives for the chosen few.

We believe that tax policy, including the work on tax extenders, should be done on a bipartisan basis. If the Republicans were truly serious about providing certainty to taxpayers, the topic of this hearing would be a full discussion of the expired tax provisions, and not just these seven tax provisions selected by the Republicans to either make permanent or provide a long term extension.

Whether or not all of the provisions should be extended deserves a full hearing. Instead, the Majority is moving ahead without any action on many important provisions.

Among them, the new markets tax credit, that encourages investment in economically distressed areas. The work opportunity tax credit to support hiring certain groups of hiring. The $250 deduction for teacher classroom expenses that is vital for schools, and the itemized deduction for state and local general sales tax, claimed by millions of individual taxpayers, particularly in states without income taxes.

Reforming our Tax Code so that it is fairer for working families encourages investment in the U.S., and raises an adequate level of revenue in the near and long term which is of vital importance.

Whether the policies put forward in the discussion draft will meet those and other goals deserves a thorough public discussion far beyond what is on tap today.

*Chairman Camp. Thank you. I would just note that in 2009 and 2011, there were many extenders that were passed by this Congress and none of them were offset. If we are going to continue to do that repeatedly, I think it is worth at least having this discussion.

Thank you, Mr. Levin.

Now it is my pleasure to welcome our panel of experts, all of whom bring a wealth of experience from a variety of perspectives. Their experience and insights will be very helpful as our committee considers the benefit of permanent tax policy for America's job creators.

First, I would like to welcome Judith Zelisko, Vice President of Tax, Brunswick Corporation, based in Lake Forest, Illinois.

Second, we will hear from Bob Stallman, President of the American Farm Bureau Federation here in Washington, D.C.

Third, we will hear from James Redpath, Managing and Tax Partner with HLB Tautges Redpath Ltd. in White Bear Lake, Minnesota.

Fourth, we will hear from Josh Odintz, Partner at Baker & McKenzie LLP in Washington, D.C., and finally, we will hear from Thomas Hungerford, Senior Economist and Director of Tax and Budget Policy at the Economic Policy Institute in Washington, D.C.

Again, thank you all for being with us here today. The Committee has received each of your written statements and they will be made part of the formal hearing record.

Each of you will be recognized for five minutes for your oral remarks, and we will begin with you, Ms. Zelisko. You are recognized and you have five minutes. Welcome.

*Ms. Zelisko. Good morning. I am Judith Zelisko, Vice President of Tax for Brunswick Corporation. I thank you for the opportunity to appear before the Committee.

Making products in the United States since 1845, Brunswick Corporation is now the world's largest maker of pleasure boats and recreational marine engines, as well as fitness, bowling and billiards equipment.

Although we have been around for nearly 170 years and are one of the long listed stocks on the New York Stock Exchange, you may know us better by some of the brands we manufacture and sell, such as Sea Ray and Boston Whaler Boats, Mercury and MerCruiser marine engines. Life fitness exercise equipment, and Brunswick bowling and billiards equipment.

We are headquartered in Lake Forest, Illinois with offices and manufacturing facilities throughout the country. Indeed, also in Asia, Canada, Europe, and Latin America.

Brunswick ended the year with approximately 15,700 employees around the world, nearly 80 percent of which are employed in the U.S.

During 2013/2014, it began or completed major expansions of several U.S. manufacturing and engineering facilities, including those in Florida, Indiana, Minnesota, and Wisconsin.

We go toe to toe with some of the best competitors around the world, many quite larger than Brunswick. We had nearly $4 billion in sales in 2013, yet we compete with the likes of Japan's Yamaha, Suzuki, and Honda. Sweden's Volvo Penta, and Beneteau of France.

We compete successfully by designing, developing, and introducing high quality products to the marketplace, products that feature innovative technology and styling. We compete by developing and maintaining low cost manufacturing processes.

We do both effectively. We rely heavily on efficient and impactful research and development, the type of innovative work that is greatly enhanced by the R&D tax credit, which we urge you to reinstate and extend, and indeed, make permanent.

To fail to extend the R&D tax credit would be to remove one of the country's most effective tools to encourage investment by business, which counts for the lion's share of R&D done in the country. The R&D tax credit spurs U.S. based innovation and R&D jobs.

As an example, at Brunswick, we have concentrated the vast majority of our design and technological developments for our more than 14 boat brands sold around the world at Merritt Island, Florida. We have a staff of nearly 200 engineers there. Within the past five years alone, the Brunswick Boat Group has secured nearly 100 patents for a number of new and innovative products.

One is called Quiet Ride, and it reduces overt noise by 25 to 50 percent. Vibration was also greatly decreased, which means a more enjoyable and smoother ride.

The R&D tax credit has been vital to our being able to maintain this drum beat and jobs. We find similar examples at Brunswick's Mercury Marine Division, headquartered in Fond du Lac, Wisconsin, this year celebrating its 75th year in business.

Research and development is a way of life at Mercury Marine, where we have approximately 400 engineers with more than 700 patents granted since 1985.

In 2012, Mercury Marine introduced the world's smallest, lightest and most durable 150 horsepower four stroke marine engine. Its popularity along with a number of other new products spurred Mercury to break ground last year for two expansion projects.

Approximately 90 percent of the project work is being performed by Wisconsin companies. These are American jobs for work that is done in America for the benefit of an American company that has been in business since 1845.

A permanent R&D tax credit provides both predictable cash flow to a company, which is important for a company's budgeting of its capital spending and research and development projects, and also prevents unnecessary fluctuations in the company's effective tax rate.

Let me explain this latter point in a little bit more detail. When the company speaks to the investment community, the company forecasts an annual effective tax rate, which the analysts then plug into their discounted cash flow and earning models.

When the tax credit expired, as it did at the end of 2013, the company has to forecast its effective tax rate without the R&D credit, which increases the company's overall effective tax rate.

If the credit is reinstated in the middle of the year and made effective at the beginning of the year, the cumulative to date impact on the R&D credit on the company's effective tax rate becomes a discrete item in the company's financial statement, in the quarter the law is effective.

Generally, analysts ignore discrete items, such items are considered unusual and non-recurring, resulting in the R&D tax credit benefit on the company's annual effective tax rate being significantly reduced for mid-year and whole year.

All this means is the permanent R&D tax credit provides certainty for the company in its annual budgeting and planning process, and results in a more constant, less fluctuating effective tax rate.

Thus, Brunswick shares the position of the R&D Credit Coalition and NAM that the Tax Code should include both a strengthened and permanent R&D tax credit and a current deduction for R&D expenses.

We also support simplifying and strengthening the credit while increasing the alternative simplified credit to 20 percent.

Therefore, we urge the Committee and Congress to reinstate and extend the R&D tax credit for 2014 as early in the year as possible, and beyond one year, to help bridge the gap to a permanent R&D tax credit.

Thank you so much.

*Chairman Camp. Thank you very much. Ms. Zelisko.

Mr. Stallman, you are recognized.

*Mr. Stallman. Chairman Camp, Ranking Member Levin, members of the Committee, my name is Bob Stallman and I am a cattle and rice producer from Columbus, Texas, and serve as the President of the American Farm Bureau Federation, representing farmers and ranchers from all across America.

Thank you for the opportunity to speak today about the importance of Section 179, Small Business Expensing, and more broadly about the merits of a stable Tax Code.

I also thank you for your leadership on tax reform. Until our Tax Code is rewritten in a simple and transparent way, it is appropriate to provide taxpayer certainty by reinstating important provisions that expired at the end of last year.

While my oral statement is about Section 179, Small Business Expensing, the Farm Bureau also supports the extension of other expired provisions, as outlined in my filed statement.

Section 179, Small Business Expensing, allows a taxpayer to deduct all or part of the cost of new or used business property in the year purchased rather than depreciating the cost over multiple years.

Qualifying property must be used in an active trader business and deduction and investment limits apply.

Farming and ranching is a capital intensive business. In order to remain competitive and profitable, farm equipment, buildings, and storage facilities must be continually upgraded and replaced. This allows agricultural producers to reduce maintenance costs, take advantage of labor saving improvements, become more energy efficient, and adopt technology that is environmentally friendly.

Smart business planning anticipates and budgets for such annual capital improvements. However, this proves challenging for farmers and ranchers because they operate on tight and unpredictable profit margins.

The immediate expensing provided by Section 179 allows farmers and ranchers to cash flow purchases that otherwise might be delayed, or that would require them to take on more debt absent that provision.

The pressure to buy capital goods at a predictable net cost is greater than ever. Newer equipment is both more energy efficient and often gentler on the environment.

We all have an interest in seeing such improvements move from the show room to farmers' fields. However, the volatile nature of farm profitability can make such investments challenging. Uncontrollable weather impacts crop yields, and unpredictable markets set the price of goods sold.

These forces can create significant fluctuations in farm income and profitability. It is not uncommon for an agricultural producer to have a very profitable year followed by multiple years of negative income.

When farmers and ranchers have good years, Section 179, Small Business Expensing, helps them to maximize available cash so they can invest more for equipment replacement.

This is why it is so important that the maximum deduction be maintained, a deduction of at least $500,000 with a phase out threshold set at $2 million.

A $500,000 limit is more modest than many might think, just as the scale of modern farming is so much larger than it once was, so too is the machinery needed to run that farm. Farmers, for instance, can easily spend more than $200,000 for a tractor or $350,000 for a combine, plus another $100,000 for a header to go on the combine to cut the crop.

Because of the sporadic profitability of most farms, investment is equally uneven. A farmer might well bunch several years of normal investment into one year if conditions warrant and sufficient cash is available. This averages out against the poor years when cash flow is not available to invest.

This reality allows farmers to make their businesses more efficient and sustainable for the long term, if the necessary tax policies are in place.

Farmers' upgrades and improvements made using Section 179 deductions help to provide some input cost certainty during periods of unpredictable profitability.

In conclusion, Section 179, Small Business Expensing, provides many benefits to small businesses, including farming and ranching. Those benefits are erased when the deduction lapses even for short periods of time.

Even as we meet here today, farmers and ranchers are holding off decisions to make capital investments given the uncertainty about renewing the expensing provisions of Section 179 that were available in 2013. There is not a lot of incentive to make these purchases if the maximum amount of $25,000 can be expensed under current law.

The Farm Bureau believes that Congress should end its practice of extending important tax provisions for just one or two years at a time. Farm and ranch business planning, which is already difficult, becomes nearly impossible with an ever changing Tax Code.

Tax uncertainty means farmers cannot truly make long term plans as long as the continuation of this provision and others remains in question.

For all these reasons, the Farm Bureau supports a permanent Section 179 small business deduction with a maximum deduction of at least $500,000, reduced dollar for dollar, when investments exceed $2 million.

Thank you for allowing us to present our views. I will be glad to take questions later from the Committee.

*Chairman Camp. Thank you, Mr. Stallman.

Mr. Redpath, you are recognized for five minutes.

*Mr. Redpath. Chairman Camp, Ranking Member Levin, and other members of the Committee, thank you for the opportunity to testify today.

My name is Jim Redpath. I am the Managing Partner and a Tax Partner at HLB Tautges Redpath, a 125 person accounting firm serving clients in the Midwest.

I have been a tax accountant for over 30 years, working primarily with closely held businesses, many of which are S corporations.

Let me begin by thanking the Committee and in particular the Chairman for his hard work to improve the Tax Code.

In our firm, we help hundreds of closely held businesses make better decisions that create value and jobs. Those efforts are hindered by a Tax Code that is simply too complex.

The rules governing S corporations are a good example. The S corporation promotes private business, capital investment, and increased employment. They are subject to various restrictions that adversely impact ownership, capital, and growth.

The Chairman's discussion draft helps mitigate some of these restrictions. I will start with the built in gains provision. In 1986, the Tax Reform Act repealed the General Utilities Doctrine and the related Section 337. These policies allowed C corporations to sell their assets and liquidate their business by paying a single level of tax. The repeal meant that for the first time there would be double tax on the sale of corporation assets followed by a liquidation.

The Tax Reform Act was a wonderful piece of bipartisan legislation, but this repeal was not. The House version included a two year rule designed to prevent avoidance of this new double tax. The Senate version had no repeal at all.

One would expect negotiations to result in an anti-avoidance rule somewhere between zero and two years. However, the final bill enacted the built in gains tax with a ten year anti-avoidance rule. This is referred to as the "BIG tax."

The purpose of the final rule was similar to the House provision, to prevent a C corporation from converting to an S corporation when a sale was eminent just to avoid the double tax.

The impact went well beyond that purpose. Today if an S corporation sells certain property or collects certain types of income before the end of the recognition period, the combined tax can be as high as 60 percent. No company willingly triggers the "BIG tax."

I find BIG tax causes many S corporations to hold unproductive assets. For example, I work with a road contractor who is sitting on old equipment out in the bone-yard rusting away that could be sold to raise capital for expanding the business and hiring more people. That investment potential is being stymied by the BIG tax.

Other clients would like to sell their businesses to up and coming entrepreneurs or employee groups, but cannot because of the prohibitive tax.

The IRS says tens of thousands of corporations convert to S corporations each year. The BIG tax effectively locks up for a decade some of the capital of these companies, limiting new investments and the creation of jobs.

Congress recognized that a ten year recognition period is too long, and has voted to reduce it three separate times, but each time the reduction has been temporary. A temporary extension forces many businesses into a difficult position. Should they sell assets or the business prematurely to take advantage of a temporary window or hold off and hope Congress extends it again?

Making the five year recognition period permanent is good tax policy, and it will provide S corporations stability and certainty so they can make business decisions that are best for the company, its owners, and stakeholders.

The other S corporation extender made permanent by the Chairman's discussion draft has to do with charitable contributions. For most taxpayers, gifts of appreciated property produces a deduction equal to the property's fair market value. S corporations who donate appreciated property will incur a future tax liability because of the way the current rules work.

This unintended result was remedied as part of the 2006 Pension Reform Act. This provision was temporary. While Congress has extended it numerous times, it expired again at the end of 2013.

Making this provision permanent would help ensure that S corporations' owners fully benefit from the value of their donations to charities.

Beyond these two extenders, there exists a significant opportunity for improving the S corporation rules to ensure that S corporations can compete with other entity types.

The provisions are part of the bipartisan S Corporation Modernization Act sponsored by Representatives Reichert and Kind.

I am pleased that the Chairman's tax reform discussion draft makes permanent several of these reforms.

Mr. Chairman, let me close by saying making permanent the five year built in gains recognition period preserves the original intent of the 1986 Tax Reform Act, and it is critical to helping corporations deploy locked up resources.

I appreciate the Chairman and the Committee for considering this provision along with all other S corporation reforms, and I look forward to your questions.

*Chairman Camp. Thank you, Mr. Redpath.

Mr. Odintz, you are recognized for five minutes.

*Mr. Odintz. Thank you. Chairman Camp, Ranking Member Levin, and members of the Committee, it is an honor to appear before you today to discuss the very important topic of two expired tax provisions, the active financing exceptions to Subpart F, and Section 954(c)(6) of the Internal Revenue Code, also known as "CFC look-through."

I applaud the Committee for making significant progress on tax reform, and I urge the Committee to make these two provisions permanent as part of tax reform or outside of tax reform.

I also appreciate that this Committee is willing to receive testimony from a former Senate Finance Committee staffer.

I am a partner in the Washington office of Baker & McKenzie. However, I appear today on my own behalf, and my testimony does not necessarily reflect the views of my firm or our clients.

Generally, the active income of an U.S. owned controlled foreign corporation or CFC, is not subject to U.S. income tax until distributed to U.S. shareholders. Under Subpart F, certain categories of income are treated as passive income and are subject to current U.S. income tax, including dividends, interest, royalties and rents.

Income from the active conduct of a banking, financing or other similar business was exempted from Subpart F until 1986. These exceptions were restored on a temporary basis in 1997.

The active financing exceptions to Subpart F currently exempts, when they come back into effect, certain income from treatment as passive income if the CFC satisfies an entity level test and a qualifying income test. The mechanics of these rules are addressed in my written testimony.

These rules are designed to reflect sound tax policies. First, banks, financing, and other similar businesses earn income that looks like passive income but is derived from an active business.

AFE appropriately treats such income as active income and ensures that such financial service businesses are treated the same as other businesses, such as manufacturers and service providers.

The entity and income rules ensure that only banking, financing, insurance, or other similar businesses receive such treatment. Financial service companies compete across the globe. AFE allows U.S. based businesses to be treated like their foreign competitors. Such competition also creates U.S. headquarter jobs that support those foreign operations.

Many U.S. based manufacturers establish financing subsidiaries that provide financing for goods sold from the United States. AFE allows U.S. based manufacturers to offer competitive financing on U.S. exports. This is a good policy.

CFC look-through provides an exception to Subpart F as well. The provision generally provides that dividends, interest, rents and royalties received or accrued by one CFC from a related CFC are not treated as passive income, so long as the payments are made out of active foreign income.

The legislative history from 2006 states that Congress enacted this provision to remove impediments to business decision making and allow U.S. based multinational corporations to deploy capital as and where needed without imposing U.S. tax.

Congress recognized that businesses are truly global and will need to deploy active foreign income to expand foreign operations to compete with foreign based multinational corporations.

These rules help U.S. businesses to fund operations in locations with the greatest potential for growth as opposed to resorting to loans from third parties.

Permanence is fundamentally important for all Internal Revenue Code provisions because virtually every corporate decision is taken after a careful review of the after tax return on investment. If the after tax return on investment is uncertain, business decisions are either delayed or not taken.

An Internal Revenue Code run by temporary tax provisions impedes legitimate business decisions and forces behavior that does not make good business sense.

Continuing a band-aid approach to these provisions undermines the congressional justification for them. Permanence is essential for U.S. based financial service sector businesses. A permanent AFE would eliminate great uncertainty regarding future tax liability. It would also allow financial service companies to appropriately price their products and services in foreign markets.

Permanence takes on added importance with respect to CFC look-through. Without look-through, taxpayers incur costs that do not advance anyone's business or make any company more competitive in the marketplace.

Permanence would eliminate these wasted expenses and allow taxpayers to effectively deploy cash where needed, recognizing that Subpart F's entity by entity rules are antiquated.

Thank you. I would be happy to answer any questions you may have

*Chairman Camp. Thank you, Mr. Odintz.

Mr. Hungerford, you are recognized for five minutes.

*Mr. Hungerford. Thank you for inviting me to share my views on the business tax extenders.

Each year, dozens of temporary tax provisions expire and many are regularly extended for another year or two with little or no scrutiny. I applaud the efforts of this Committee to scrutiny the tax extenders.

Let me summarize my main points. First, the tax extenders package is being considered in a challenging fiscal environment of budget deficits as far as the eye can see, in which maintaining long term fiscal discipline is necessary.

Second, making some or all of the expiring tax provisions permanent without offsetting the revenue losses will permanently increase budget deficits and accelerate the accumulation of Federal debt.

Third, running large annual budget deficits when the economy is operating at or near its potential can accelerate inflation, increase interest rates, reduce private sector investment, and reduce economic growth. Thus, destroying jobs.

It is likely that any jobs created by these seven tax provisions would be entirely offset by jobs lost due to larger budget deficits over the longer time.

In the time remaining, let me expand on these points. After 2023, we face the unsustainable growth of Federal debt as projected under CBO's extended baseline, a baseline that assumes these seven tax provisions, as well as 50 to 60 other expired provisions, are not extended.

Between now and 2023, Federal debt rises from 72 percent of GDP to 78 percent. Barring tax and spending changes, Federal debt as a percentage of GDP is projected to grow to over 100 percent by 2038 and to an unprecedented 200 percent by 2080.

Concern over long term fiscal challenges appears to have made long term fiscal discipline a priority.

Chairman Camp recently unveiled a comprehensive tax reform plan that is revenue neutral over the ten year budget window. Revenue losses from tax rate reductions and making certain tax provisions permanent, including most of the provisions under discussion today, are offset with revenue increases from base broadening.

The advisory for this hearing, however, notes that revenue neutrality is not consistent with recent practice by Congress in its consideration of tax extenders legislation.

I am left to wonder if the commitment to long term fiscal discipline is being abandoned for this extenders package.

Let me examine the budget implications of the seven provisions under discussion today, which account for almost half of the revenue loss of all expiring tax provisions.

Making these seven tax provisions permanent with no offsetting revenue increases would add over $200 billion each year to the deficit, thus adding over $200 billion to Federal debt by the end of 2023, almost one percentage point of GDP.

Even a two year extension as proposed by the Senate Finance Committee, would add almost $50 billion to Federal debt by 2023, and modifying some of these provisions, as Chairman Camp has proposed, can reduce the revenue losses somewhat, but the overall consequences are similar, a large increase in projected Federal debt.

If long term fiscal discipline is abandoned, then we face a future of budget deficits that are larger than expected.

Research suggests that running large annual budget deficits in perpetuity can have adverse economic consequences, thus destroying jobs, and as I mentioned before, any jobs created by these provisions would likely be entirely offset by jobs lost due to larger budget deficits over the longer term.

Given the long term fiscal challenge we face, I believe that whatever is decided about these provisions, the decision should not increase projected budget deficits. The tax extenders should be paid for by increasing tax revenues.

Thank you. I would be happy to answer any questions you may have.

*Chairman Camp. Thank you. Thank you all for being here and thank you for your statements.

I have a question. Every time Congress has considered a short term extenders package, the Joint Committee on Taxation, which is our referee in these matters, estimates that the provisions will actually cease to exist. They look at the costs and say these provisions are not going to be continuing.

However, with spending programs, on the appropriations side, those are always assumed to go on forever. Even if they expire, they assume they are going to go on forever.

The Congressional Budget Office estimates that further extensions of spending have no cost, but yet with tax policy, the estimates say further extensions of current policy do have a cost.

There is a difference of treatment in terms of tax relief and spending which creates a bias in my view, a bias against extending expiring tax programs in favor of extending expiring spending programs.

If you look back at history, Congress virtually never pays for extenders, including those like the R&D tax credit, which supposedly have been temporary since 1981.

My question is this, given the repeated extensions, is not treating long-standing features of the Tax Code as if they were permanent certainly a fundamentally more honest way, accurate way, frankly, and more transparent way of looking at the costs and benefits of these policies?

Mr. Odintz, I just ask for your opinion on that.

*Mr. Odintz. Looking at it from a business perspective, businesses cannot rely on provisions when they analyze whether to move cash from one location to another or to engage in a transaction.

They can only rely on current law and cannot rely on law that may or may not be extended, as you noted, the R&D credit has been extended since 1981, there is an exception there where it expired, so taxpayers could not enjoy the credits during that period of expiration.

I look at these issues from a business perspective and it is difficult for businesses to make decisions without permanence or at least to understand how long these provisions will be in effect.

*Chairman Camp. Mr. Redpath?

*Mr. Redpath. I started my career in 1981, and have dealt with these extender provisions for years. It makes businesses do things they would not otherwise do.

We have a temporary window of opportunity and it makes us make tax motivated decisions versus business decisions that may not have been made had we not had to deal with the expiration of the tax provisions.

*Chairman Camp. Again, Mr. Stallman?

*Mr. Stallman. Farmers and ranchers deal with extensive uncertainty. It would be preferable to have more certainty with respect to the Tax Code as has been referenced by my colleagues.

Farmers are making these decisions based on what they know, and right now, without clear certainty about what the future is of some of the extender provisions, particularly the Section 179 expensing provision, that is hindering or at least slowing down their decisions to make these expenditures and

investment, which are important for maintaining an agricultural productive base, and frankly important for manufacturers and all the jobs created by those who create this equipment.

*Chairman Camp. Thank you. Ms. Zelisko?

*Ms. Zelisko. Having a permanent R&D tax credit, which I was focused on this morning, really helps business to be able to predict its cash flow.

In the planning process, when you are looking at R&D projects, they can span four to five years, having that certainty is critical in determining whether that cash flow is there or not.

Relying on a credit that basically has an extension of one or two years and might not even be there obviously is not part of that process. It cannot be, you need to have predictability, you need to have certainty.

With regard to cash flow, which is important in determining the amount of funds you are going to be able to set aside for those research projects, it is important to be able to know that the R&D credit would be around for business.

In addition, there is also financial implications I mentioned in my written statement and in my oral testimony, with regard to how the investment community looks at a publicly traded company.

When you are looking at whether or not an R&D credit is available, that impacts your effective tax rate. Why is that important? Analysts take that effective tax rate and factor it into their financial models.

Why is that important? It is the analysts that determine what they are looking to forecast your earnings per share. Your earnings per share are on an after tax basis. They take that earnings per share and then use a multiplier which they attribute to your particular company, depending upon the industry and what its history of earnings have been, and then they come up with basically a share price and a range, which then they use for their buy side and sell side analysts with regard to your stock price.

Again, predictability is so critical in this area and permanent tax policy would enable that to occur.

*Chairman Camp. We have had dozens of hearings over the last four years in this Committee where we have heard from many witnesses who said investing in their businesses and effectively planning for the future requires certainty. I heard all of you mention that as well, and especially when it comes to tax policy.

Each of you mentioned how some of these temporary tax provisions affect your companies and clients and some of your members.

What is your sense in terms of the economic benefit if businesses could generally rely on tax rules which would or would not be permanent going forward? What do you think sort of the overall economic impact might be if you can?

Ms. Zelisko, I will start with you and go the other way.

*Ms. Zelisko. Thank you. Certainly, having certainty with regard to the R&D credit, I think, has a tremendous multiplier effect from an economic standpoint.

When you are basically able to invest and create new products, which again accepted in the marketplace, you are providing not only jobs and developing those products, you are providing sales revenue.

Therefore, you are able to further invest in your company, and that means jobs. Jobs mean housing. Housing means there are businesses in a particular community that are going to thrive.

Therefore, I think definitely the multiplier effect is often missed when you are looking at permanent tax policy and the certainty it provides.

*Chairman Camp. All right. Mr. Stallman?

*Mr. Stallman. Agriculture is very similar. You have to maintain your productive base. You have to make capital investments to do that. Having certainty about tax policy allows that planning to occur. Without that, you are sort of delayed and behind the curve, if you will, from deciding how and when to make these investments that erodes your productive base.

Our agricultural export surpluses are certainly contributing to our balance of payments. The jobs that are created through that activity as well as the internal production and the amount of products and inputs that we purchase from suppliers, all of that creates great economic activity.

With tax certainty, you have more of that. With tax uncertainty, you have less of that.

*Chairman Camp. All right. Mr. Redpath?

*Mr. Redpath. Let me answer that with an example. I was working with a client last year, and in 2012, their five year S corp built in gains recognition period expired. They had an opportunity in 2013 to take advantage of the temporary rule of five years.

They owned millions of dollars of pipe in Western Minnesota that was subject to the built in gains tax, that they would need to sell in 2013 in order to benefit with regard to the current temporary five year rule.

This is the kind of pipe that you cannot sell in a year. It really impacted their decision. What do they do with this pipe? Do they sell it for less than they should sell it for? Can they make a business decision? Can they hope you extend it to 2014 and beyond?

What they ultimately had to do was sell some of this pipe for less than the real value of the pipe in order to move it to take advantage of the temporary window with regards to the five year recognition period on built in gains.

*Chairman Camp. Thank you. Mr. Odintz?

*Mr. Odintz. Sure. I would like to also provide an example. U.S. manufacturers frequently establish a foreign subsidiary for financing their products, and as you may know, in banking or a similar business, the margins can be pretty low, interest rates on loans take into account after tax returns on that product.

For an U.S. manufacturer, it is important to have an interest rate that is competitive in the marketplace. If the U.S. manufacturer cannot rely on pricing of that interest rate as being competitive, then they may not get the financing for their widget and may lose on a sale of their widget and a foreign manufacturer may get the transaction.

I cannot tell you the macro effects, but on a business by business effect, these rules have significant impact.

*Chairman Camp. All right. Thank you. Mr. Levin?

*Mr. Levin. Thank you very much. Welcome again.

Let me just kind of go down the line, if I might, and start with you, Ms. Zelisko. As Chairman Camp mentioned, I very much favor the extension of the R&D tax credit. We have been working on this.

I would like to ask you, do you know what the Joint Tax cost would be of permanent extension?

*Ms. Zelisko. I do not have that number currently available. I know it is significant. Again, I think from a tax policy standpoint, it is important.

The country back in 1981 when it put this credit in place really led the world as far as being ahead of the curve and realizing the importance of providing incentives for businesses to invest in research and development.

*Mr. Levin. I agree. I have been one of the most active proponents. I just wanted to ask you about the cost.

Mr. Stallman, on the small business expensing, do you know what the Joint Tax ten year estimate is for making it permanent?

*Mr. Stallman. I will have to concur with my colleague, I do not know that specific number. Once again, in terms of tax and economic policy, the provision itself is very important, I believe, in generating additional economic activity and thus, generating extra revenue in terms of tax revenues.

*Mr. Levin. For R&D, their estimate is $76 billion. For expensing, it is $69 billion.

Mr. Redpath, you come off more easily. Do you know what the estimate is for your provision?

*Mr. Redpath. No, I do not, but I work closely with many S corporations that have potential built in gains tax exposure. As I said in my oral testimony, no one willingly pays the BIG tax. They structure transactions, they structure operations in any way they can to avoid it, which ultimately ends up tying up assets for ten years or more.

*Mr. Levin. You stated the merits. I think there is much to be said for each of your testimonies. I just wondered about the cost.

Mr. Odintz, I am going to ask you, you mentioned two of them, the CFC and also active financing. We have been working on these two issues forever.

Do you know what Joint Tax projects as the cost, ten year cost, of making this permanent?

*Mr. Odintz. Sure. I believe for CFC look-through, the cost is around $10 billion over the ten year window, and then for AFE, I believe the cost is in excess of $50 billion over the ten year window, but under $100 billion.

*Mr. Levin. According to Joint Tax, their estimate for ten years for the CFC provision is $20 billion plus, and for active financing, it is $70 billion. You are pretty close, but 10 to $20 billion is a lot of money.

I just want to mention that because as I said in my opening statement, I think we need to look at these issues in a holistic way, and not only these specific ones, but others that are not being looked at, and I think the issue of cost, no matter how you try to shape it, is indeed relevant.

I yield back.

*Chairman Camp. Mr. Johnson?

*Mr. Johnson. Thank you, Mr. Chairman. I did not get a chance to tell you but I want to take this moment to thank you for your service and in particular your tireless effort in advancing the cause of tax reform.

*Chairman Camp. Thank you.

*Mr. Johnson. Ms. Zelisko, I have a number of questions I would like to ask you about the R&D tax credit. First, to begin with, we have heard that the potential for long drawn out fights with the IRS over the R&D tax credit can discourage companies from even claiming the credit.

Has Brunswick faced similar fights with the IRS?

*Ms. Zelisko. We have had some disagreements with regard to the R&D tax credit with the IRS. Basically, one of the challenges that we face is that often times the IRS wants to basically think that you should keep your books and records such that they are on a project by project basis with regard to these R&D projects, as opposed to we keep our books and records on a cost center basis.

The IRS wants to directly be able to point to the different costs involved in the R&D effort to a particular project as opposed to taking a more reasonable approach in an allocation that would be supportable but would make more sense.

Often times, that is where we have faced our challenges.

*Mr. Johnson. You are saying the IRS is not reasonable. I have to agree with you.

Do you have any more thoughts on how to make the credit more taxpayer friendly?

*Ms. Zelisko. I think basically looking at the alternative simplified credit, where you basically would eliminate some of the controversy that taxpayers have been challenged with with regard to the base period, a receipts calculation, you are talking about a base period that goes back to 1984 to 1988, where you are looking at data that is 25 to 30 years old.

If you are in a company that has bought businesses and sold businesses where you have had that research and development in those years, you have to adjust for that.

Needless to say, that probably makes it at best problematic in trying to track that.

I think when you are going to an alternative simplified credit, you are looking at data that is two to four years old, a lot more manageable than 30 years old.

*Mr. Johnson. As you may know, in Chairman Camp's tax reform discussion draft, the R&D credit is modified so it is based on the alternative simplified credit, ASC, rather than the traditional credit.

Do you have any thoughts on how shifting to the ASC would improve the R&D credit?

*Ms. Zelisko. As I said, I think basically it would eliminate the controversy around the base period by going to an alternative simplified credit.

I would urge the Committee and Congress to not eliminate supplies, the deduction for supplies and software, because for our company, supplies can be anywhere from 20 to 25 percent of our total qualified research expenditures.

When we are making a new engine, you basically destroy a lot of prototypes in that process when you are getting it right.

I would urge the Chairman and Committee to rethink the supply issue with regard to deductibility.

*Mr. Johnson. Do you think changes like that would make it easier for companies to claim the credit generally?

*Ms. Zelisko. We have found when the IRS actually goes out and visits your facility and they talk to the engineers that are basically involved in the process, they truly realize what R&D is all about, as opposed to sitting back in a field office in a vacuum.

*Mr. Johnson. You think some of them do that? Thank you so much. Thank you, Mr. Chairman.

*Chairman Camp. Thank you. Mr. Doggett?

*Mr. Doggett. Thank you very much, Mr. Chairman. Despite all the talk about tax reform that will be more simple and equitable and tax reform that will not dig us deeper into debt, Republicans have chosen to first not introduce that legislation.

They have had reserved since January of last year, H.R. 1, for comprehensive tax reform, and as of today, it still shows H.R. 1 is reserved for the Speaker.

Instead, today's hearing is about borrowing more money from the Chinese to maintain some very complex corporate Tax Code provisions that depend upon their very complexity to work.

The controlled foreign corporation provision and the active financing provision are all about this Congress picking winners and losers rather than leaving the marketplace to decide.

They lower the effective corporate tax rate for some businesses and say to some businesses they do not have to pay as much for the cost of our national security and other vital services as their neighboring corporation that is competing and paying a higher effective tax rate.

Mr. Hungerford, I want to ask first about the active financing provision. We understand that would take borrowing about $70 billion of additional debt over the next ten years to maintain.

Under existing law, if a financial institution makes a loan to a domestic corporation, to one of Mr. Stallman's farmers, to a company that is making it in America, manufacturing here, as I understand it, it reflects in its corporate tax return the interest that it earns from extending the loan and it deducts whatever the cost of extending that credit might be, and it pays taxes on the difference. Is that right?

*Mr. Hungerford. That is correct, and thank you for asking the question.

*Mr. Doggett. If it is a loan or some other form of credit to a company that is not making it in America, that is a foreign operation, then it can take its expenses now for extending the credit and take its profit on its earnings whenever it feels like it.

Is that not essentially what the active financing provision allows?

*Mr. Hungerford. The active financing exception is an exemption to Subpart F. If this income was all considered Subpart F, it would be taxed immediately.

*Mr. Doggett. Yes. The very fact that we are talking about Subpart F and the exception to Subpart F and active financing and whether it is active or passive is the kind of thing that does add complexity and causes the eyes of most people to glaze over rather than to look at the effect of what the provision is, which is to provide, is it not, Mr. Hungerford, a substantial subsidy to encourage the export of American capital and American jobs rather than to invest in making it in America?

*Mr. Hungerford. Yes, that is correct.

*Mr. Doggett. As far as the controlled foreign corporation provision, and the CFC look-through exception is concerned, another $10 billion that we would borrow from the Chinese, if you have two companies right next door to each other and one of them can afford a bunch of fancy accountants and consultants and high priced lawyers to rig up some corporate fiction that they have a subsidy in the Bahamas or Bermuda, they can license their patents, their copyrights, perhaps their trademark name, to a tax haven company, and strip off earnings that they have had right here in America, that their smaller neighbor does not do.

The effect of that is to lower their profits by increasing their costs in some tax haven. Is that not the way it works?

*Mr. Hungerford. Yes.

*Mr. Doggett. In fact, using both of these devices and many other complex provisions, over the last decade I believe GE has not only lived better electrically but they have managed to pay an effective corporate tax rate of less than two percent, two cents on the dollar, which is a deal that any hard working American or business would love to have.

*Mr. Hungerford. That is correct.

*Mr. Doggett. Essentially, repealed their taxes except at a certain minimum level.

Under these controlled foreign corporations, you actually end up with what many people have called "stateless income." How does that work?

How does some income just never get taxed by any entity either here in America that contributes to the cost of our national defense or by anyone else?

*Mr. Hungerford. Part of it is through the CFC look-through rule that income can be shifted, that is from a high tax country, high tax foreign country, to a low tax foreign country, in such a way that it is not taxed in that high tax foreign country, and the transaction is not taxed by the United States.

*Chairman Camp. All right. Time has expired. Thank you. Mr. Brady is recognized.

*Mr. Brady. Chairman Camp, thanks for your leadership, tireless leadership, to fix this broken Tax Code and reign in the IRS, get this economy going.

This hearing is about jobs and we need them so badly. This is the worst economic recovery in 50 years. Millions of people have given up looking for work. Millions of work cannot find it. It has taken six years just to break even on the number of jobs along main street.

Today, proportionately, fewer Americans are working than when this recession ended. We are actually going backwards.

Those who are being hurt most are women and young people and those just graduating from college. We ought to be focusing on jobs.

What I hear from our witnesses today is that these tax provisions are critical to creating jobs, and they are less pro-growth if they are temporary, and far more pro-growth if they are permanent, and businesses of all sizes can count on them, from innovative businesses doing research and development to investing in America with those jobs, or small businesses and family farms and ranchers creating jobs here in America.

About the CFC look-through that allows American companies to be competitive against China and Europe and Latin America, so we can create jobs here in America.

This is what this hearing is all about. While I appreciate the concern about fiscal responsibility, what Chairman Camp has shown in his discussion draft is you can lower rates, you can make this Tax Code more pro-growth without adding a dime to the deficit.

This really is about removing an asterisk around these temporary provisions in the Code so we can grow the economy more.

Chairman Johnson has asked about the research and development area, which I have an interest in, as all members do. I want to talk about small business expensing.

Right now, one of the missing ingredients in this recovery, one of the reasons it is so weak, is that businesses are not able and do not feel comfortable to reinvest back in new equipment, software, and technology.

I want to ask first Mr. Stallman and then Mr. Redpath, how important it is -- we need big businesses to invest and we need small businesses to invest.

I want to ask both of you gentlemen how important is it that our businesses be able to expense, you know, that $500,000 figure, and how important is it that it is made permanent so they have that certainty? How important to the economy is it?

Mr. Stallman?

*Mr. Stallman. From a farming and ranching standpoint, we believe it to be very important. I referenced the high cost of equipment that exists. I did not mention the cotton pickers that are $600,000 to $750,000 at a pop now.

The point is we need the $500,000 expensing. This is not about tax avoidance. This is just changing when you pay the tax because you are just accelerating the expense for that year. It helps provide additional cash flow. It helps you make that decision, and having certainty about that is what allows you to move forward.

Just a personal example, I am right now thinking about having to replace a tractor on my farm. I am going to wait and see what happens with these tax extenders and what happens to the provision for Section 179 expensing before I make that decision.

*Mr. Brady. When you buy that tractor or cotton picker, it certainly reverberates through the economy, does it not?

*Mr. Stallman. Absolutely, all the way from the raw materials suppliers to the manufacturers to the dealers selling it to the people that service it, just all the way down the line.

*Mr. Brady. Thank you. Mr. Redpath?

*Mr. Redpath. Thank you. Two things. One is to answer your question also answers the question why we should extend the built in gains tax period. That will free up the capital necessary to make those expensing acquisitions.

I look at the expensing provision as a provision that absolutely works, and the reason it works is everyone that qualifies for it uses it. It is one of these provisions that is in the Code, and if they qualify, they use it, so it must work.

For my clients, spending those investments is how their companies grow. When companies grow, they create more jobs.

*Mr. Brady. Mr. Chairman, thank you for hosting this hearing. I know we have members wanting to inquire about a number of the other provisions. Thank you for holding it.

*Chairman Camp. Thank you. Mr. Lewis?

*Mr. Lewis. Thank you very much, Mr. Chairman, and thank you, Mr. Chairman, for holding this hearing.

Mr. Hungerford, in your testimony you raised the importance of long term fiscal discipline. You also highlight the question or objective of a tax break.

When considering tax extender and tax reform, what action by this Committee would cause the least economic disruption?

*Mr. Hungerford. I think two things the Committee could be doing. One is determining which provisions belong in the Tax Code and which do not. I think there is a lot to be said from both a business standpoint and a budgeting standpoint to make them permanent.

*Mr. Lewis. In your work, do you believe that a broad or a narrow lens should be applied when considering tax policy and why?

*Mr. Hungerford. I think as broad a lens as possible. You need to take into account other things in the Tax Code. Also, you need to take into account the whole budget situation, basically spending and the revenue side.

I am concerned over the long term about deficits and unsustainable accumulation of debt.

*Mr. Lewis. Thank you very much. I thank the other members of the panel for being here. I yield back, Mr. Chairman.

*Chairman Camp. Thank you. Mr. Tiberi?

*Mr. Tiberi. Thank you, Mr. Chairman. Mr. Stallman, welcome. I understand you hail from Columbus, Texas. I hail from Columbus, Ohio. Good to have two Columbus guys in the room.

Mr. Brady posed a question regarding Section 179, and you gave your tractor example. If you could just go a little bit further on what ranchers and farmers have done in reaction to what was the law at the $500,000 expensing level. We know what they have not done because of the new amount of $25,000. What do you believe would happen if we extended permanent law to the old limit of $500,000 in Section 179?

*Mr. Stallman. I will tell you this anecdotally based on my conversations with farmers. There were a number of them that accelerated their purchase decisions prior to December 31 because they had certainty up to that point. They were uncertain about what was going to happen after that.

Right now, I would suggest there are a number of them that are in a holding pattern waiting to see what happens before they commit the funds to purchase equipment in excess of what the $25,000 deduction would allow.

If it were made permanent, that would create the certainty, I believe, for farmers and ranchers to do that very necessary planning for their capital structures or capital improvements that they need to maintain a productive farm and ranch.

I think it would unleash dollars that frankly have been held given the fact that we have had a good agricultural economy, and that is subject to change obviously, but we have had a good economy where farmers and ranchers have had some profits and some cash.

They are waiting to see what they are going to do with that.

*Mr. Tiberi. I have heard the same thing anecdotally from small business owners in my District of Central Ohio, and plan on introducing a bill that would extend this permanently, a bipartisan bill, later this week.

I know your organization is supportive of that, as are many other small businesses. Thank you for being up here today from Columbus, Texas.

Mr. Odintz, on another matter that Mr. Doggett brought up, reading your testimony, I think you have a different view on the active financing exception.

Can you talk about the process that you and your clients go through because of the temporary nature of this provision in the past, and how this is much like 179, a provision that actually helps American competitiveness, a little bit different than what we heard a little bit ago?

*Mr. Odintz. Sure. I think it is important to note that AFE does not export jobs. What it does allow is for a bank or similar business to establish a branch or to establish operations in a location.

If you think about it, when people go to a bank, they like to walk into a physical bank. It is important that the U.S. headquartered banks can establish a local operation that facilitates the relationship with clients.

If the rules do not exist, then it is difficult for clients to price out loans, certificates of deposits, and other like instruments at a competitive rate with foreign based multinational's that have operations, real physical operations, in the same jurisdiction.

As far as jobs, a lot of companies, U.S. based multinational's, manage their foreign currency risk and other international risks in their headquartered location, so that happens in the United States, so there is a knock on effect of jobs when an U.S. based bank opens operations abroad and is unable to manage its risk domestically.

*Mr. Tiberi. Correct me if I am wrong, this allows U.S. financial services companies that do business all over the world to be competitive with their foreign competitors and treats them exactly like non-financial services companies are already being treated under the law.

*Mr. Odintz. That is correct. AFE merely treats a bank or other financial service provider like a manufacturer. It does not provide a better position vis-a-vis Subpart F. It just treats them equally like non-financial service providers.

*Mr. Tiberi. It does not allow for any deferral of profits in the U.S.?

*Mr. Odintz. That is correct.

*Mr. Tiberi. Why do you think it gets attacked?

*Mr. Odintz. I think the discussion sounds like a greater discussion on whether we should have deferral, which is a different discussion, but to the extent we are going to retain a system that has deferral, I do not see a reason to distinguish between banks that engage in active business versus a manufacturer that makes widgets.

*Mr. Tiberi. My time has expired. Thank you so much.

*Chairman Camp. Thank you. Mr. Kind?

*Mr. Kind. Thank you, Mr. Chairman. Thank you for holding this hearing, and we appreciate the witnesses' testimony here today.

Let me just start with a general question for the panel. Other than Mr. Hungerford, who testified pretty clearly that he thought that extension of these expired provisions without paying for them may be detrimental to economic growth in the future, does anyone else on the panel have any concerns about the potential lack of offsets to pay for these expired provisions as we move forward?

[No response.]

*Mr. Kind. Not really? One of the hardest things we have to do around here, whether it is new program spending or whatever, is finding offsets in order to pay for things so that we are not adding to the deficit, especially in future years, the "out years" as they say.

I think that is going to be an issue that we are going to have to have an ongoing conversation about with the extension.

Mr. Stallman, appreciate your testimony on the importance of 179 expensing. Obviously, I come from a large agricultural area in the State of Wisconsin. I have been working with Mr. Tiberi in introducing some legislation along those lines, a permanent extension of 179, indexing it for inflation.

What we are thinking about doing though is taking the $500,000 and lowering it to $250,000 for real property, but still indexing it. Would you have any concerns with that, as it would affect real property?

*Mr. Stallman. Are you talking about the single purpose buildings?

*Mr. Kind. Yes.

*Mr. Stallman. $500,000 would be better, obviously, because these buildings, particularly with the technology and the systems that are put in place now are getting more expensive, not less expensive. I think that is the issue there in terms of the growth and cost of these kind of single purpose buildings.

*Mr. Kind. I do not know if you have or someone at Farm Bureau has had a chance to really go through the Chairman's discussion draft that was introduced a couple of weeks ago, but in it, they are calling for the elimination of Section 1031, the like-kind exchanges.

Have you had a chance to look at that and what the impact might be in the agricultural section if we eliminated like-kind exchanges?

*Mr. Stallman. We are reviewing the whole proposal now and trying to get sort of the big picture of what it means for agriculture and all the tradeoff's that are there.

I will tell you that our policy supports maintaining the 1031 exchanges. Those have been very useful for farmers and ranchers as they have gone about planning for the future, as they have gone about trying to expand their operations, plus important for those who may want to move on and do something else but want to try to manage the tax consequences of selling their land.

*Mr. Kind. I would like to stay in touch with you and get some more feedback on what the impact might be, especially in the agricultural field.

Mr. Redpath, appreciate your testimony, too, as far as the impact on S corporations and the five year BIG holding period, something that Mr. Reichert and I have been working on with our S corp modernization bill.

You also indicate in your testimony that you think we need to expand the qualifying beneficiaries to include non-resident alien individuals as well. Could you explain why you think that is necessary?

*Mr. Redpath. Yes, thank you. The provision relating to the non-resident alien individuals deals with who can be permissible beneficiaries of electing small business trusts, which are eligible S corporation shareholders.

It does two things. One, it puts S corporations at par or closer to par with LLCs, their competing flow through model, where LLCs are not restricted to the types and numbers of owners and the types of ownership.

This would allow S corporations to attract non-resident alien foreign owners through trust only.

In that provision, the trust actually pays the tax, and it pays the tax at the highest individual rate. Some of the positions are who cares who the beneficiaries are, the trust is actually the taxpayer.

The second and more important provision that I run into with regard to this provision is family business. More and more of our family businesses are resulting with non-resident alien family members, who without this provision cannot enjoy the benefits of family ownership of the family S corporation.

*Mr. Kind. One other thing, Mr. Redpath. The five year BIG holding period and the impact on the charitable deduction provisions, can you explain in a little bit more detail what impact that has?

*Mr. Redpath. Yes. I will just give you an example. Let's assume an S corporation has appreciated property that it wants to donate to a charity, whether it is appreciated securities or land or a building, and they want to donate it to a charity.

When they donate to that charity, they get a deduction for the fair market value of the property, just like anyone else, like an LLC or C corporation or individual, but they are required to reduce the basis in the stock they own by that full fair market value.

All other taxpayers get to reduce by the basis of the property, which is substantially less than that. It results ultimately in not being able to deduct the full fair market value of the property.

*Chairman Camp. All right. Thank you. Time has expired.

*Mr. Kind. Thank you.

*Chairman Camp. I am going to go two to one now, Mr. Reichert.

*Mr. Reichert. Thank you, Mr. Chairman. I want to add my thanks to you, too, for pushing forward with tax reform over these last three plus years, and in fact, thanks to the entire Committee because this has been a bipartisan effort, over 40 hearings and meetings after meetings after meetings after meetings.

[Laughter.]

*Mr. Reichert. On tax reform. It has been a little bit in contrast to some of the other major bills that were passed in previous years, but this is an effort to reform the Tax Code, and the people on this Committee know how hard that is. You certainly know how hard that is, since 1986, we have been hoping for this. People in this audience know and I think people around the United States understand how critical this is and how difficult this is.

The whole goal here is to create a tax reform bill that energizes business, and as Mr. Brady says, creates jobs. We do not work for the IRS any longer, but the Tax Code works for us, right? That is the goal.

There are a couple of things I want to touch on, Ms. Zelisko, both in your oral and written testimony. First, the need for the permanence in the R&D credit for the U.S. to be competitive on the international level.

Second, your concerns that eliminating supplies and computer software from the credit might have unintended consequences.

On your first point, in Washington State, we do not have to look too far to see what other countries are doing to attract R&D. You may already know this. In Canada, not only have they reduced their Federal corporate income tax rate to 15 percent, they have now a permanent 15 percent credit on research and development activities that applies to all expenditures and special accelerated depreciation rules that apply to so-called "research assets."

On top of this, the various provinces and territories have added their own research tax incentives. For example, in British Columbia, right above the State of Washington, there is now a ten percent credit for all companies, on top of the Federal incentive.

On your second point, the unintended consequences of removing software and supplies from the credit, we have heard a couple of things, that no other country in the world specifically denies R&D credit eligibility for all software costs and secondly, for manufacturer supplies, such as test models, can be an integral part of conducting scientific research.

Could you please comment on both the importance of the permanence in the R&D credit to stay competitive on an international level, and the potential unintended consequences for removing expenditures on software and supplies for the tax credit?

*Ms. Zelisko. Yes. The United States has the opportunity to lead once again in this area. We did in 1981, but that recent OECD study ranks us now 22nd as far as the incentivization the R&D credit provides here in the U.S., when it is in play.

I think therefore making it permanent is going to really accelerate and innovate and provide the incentive for businesses to plan, to be able to decide that we are going to be able to do that extra project as a result because we know that the cash flow is going to be there, and it is not going to be on again, off again.

I think with regard to that, ranking number one in 1981 and now 22nd, obviously that says something, that we need to basically take notice and lead as opposed to trying to catch up.

In that regard, with regard to the amount of items that should be allowed as far as qualified research expenditures, having supplies and software being part of the equation which it was until the proposal here we have before us, I think that is important.

Supplies are critical as far as when you are doing research and development. Obviously, wages are the majority, as evidenced by the research and development credit; 70 percent of all expenditures relate to wages. That means 30 percent relates to supplies, not an insignificant amount.

I think if we want to be competitive as opposed to regressing and taking a step back, retaining supplies as a deductible, as a qualified research expense for the R&D credit, is so important, along with software.

Software is critical. Look at the developments of the companies we have had here in the United States where software development -- we lead in that forefront, and I think we want to retain that.

*Mr. Reichert. Thank you. I yield back.

*Mr. Young. [Presiding] The gentleman's time has expired. Mr. Boustany is recognized for five minutes.

*Mr. Boustany. Thank you, Mr. Chairman. I am very pleased we are having this hearing today and happy that we are focusing on a bipartisan tax provision that I have long championed, and that is making the CFC look-through permanent.

You can argue that a lot has changed since 1962 when a lot of these international provisions were written.

Mr. Odintz, I think you pointed out that Subpart F is antiquated because it sort of assumes that business is done country by country, on a country by country basis, and does not take into account the global nature of business today, the type of environment that U.S. owned businesses are trying to compete in.

These are companies going up against -- these are American companies that create value, they create American jobs, and they are going up against foreign competitors.

You pointed out in your testimony a couple of things. One, the concept of making this permanent so there is certainty for these companies, our U.S. companies, to plan and make sound business decisions, and you also talked a lot about the competitiveness of American companies vis-a-vis our foreign competitors.

This provision is not well understood. I think we heard from the other side just a little while ago some relative misunderstanding about how this works in this 21st Century economy, and why it is necessary for U.S. companies.

The CFC look-through allows payments of dividends, interest, rents or royalties in the normal course of active business operations between U.S. owned foreign subsidiaries, so they can deploy capital without an immediate tax burden in their normal business operations, and it does not apply to passive highly mobile income. That is an important distinction.

I want to give you an opportunity to expound further on this. Some have voiced concerns that the CFC look-through rule allows U.S. companies to avoid taxes on their foreign income.

If the rule only applies to active foreign income that otherwise is not subject to current U.S. income tax, is this not really just about foreign taxes and not U.S. taxes? Is it really at the end of the day Congress' responsibility to force American companies to pay higher taxes to other countries?

*Mr. Odintz. Congressman, I think you have correctly pointed out that in order to use the provision, it requires the payments out of active income. The issue really is whether the U.S. should have a current inclusion of that income or the taxpayer should get a deferral for redeployment of capital to another location outside the United States.

That is the issue. I look at it not as a provision designed to enable stripping from one country to another but rather for flexible utility of cash.

If you look at U.S. multinationals, they are limited in how they can conduct operations. Without CFC look-through, they have to separate jurisdiction by jurisdiction or country by country, and when you look at the EU, for example, the European Union is one zone, but yet U.S. rules require U.S. corporations to treat each country separately and distinct, which is certainly not how European competitors or other competitors look at the EU.

*Mr. Boustany. Thank you. I know when Congress enacted the provision in 2006 it wisely recognized that it would really create a level playing field for U.S. companies, but talk a little bit more about the competitiveness, in the time I have remaining.

U.S. companies trying to operate in a 21st Century global economy, a very competitive global economy, give us more background from that perspective.

*Mr. Odintz. Sure. On the competitiveness piece, cost of capital can be expensive and obviously if a company can move funds from one jurisdiction to another by a dividend as opposed to having to borrow from a third party, the cost of capital is lower, and it can be more efficiently deployed to a market where there might be a new opportunity.

For example, in an effort to expand in one country in the European Union that was untapped, it allows the U.S. company to deploy that capital in that place and open a new facility or sell into that marketplace and compete with the same cost of capital as a foreign competitor.

*Mr. Boustany. This supports American jobs; right?

*Mr. Odintz. Yes, it does.

*Mr. Boustany. Thank you. That is all I have.

*Chairman Camp. [Presiding] Thank you. Mr. Pascrell?

*Mr. Pascrell. Mr. Chairman, thanks for bringing us together. I think this is a very important hearing. As we have heard today, companies want certainty. Individuals rely on you and rely on that certainty.

There are many extenders not on the agenda, about 50 of them. I hope they will get a fair hearing as you are getting a fair hearing today.

We can address the new markets tax credit, the mass transit tax benefit, the work opportunity tax credit, which has bipartisan support, and various other provisions.

I support the goal of coming up with a permanent solution to the tax extenders. Like many other things here in Congress, this issue comes up every year or two, and instead of finding a way to solve it once and for all, we kick it down the street.

The sustainable growth rate is a perfect example, SGR. We debated it last week and passed it. We had the momentum. We had the lowest score to repeal the formula in years, but we did not have an agreement on how to pay for it, but we are trying.

That is the crux of the issue with extenders. We need permanence in our Tax Code, but we cannot sacrifice the progress we have made bringing down our deficits, which have come down at the fastest rate since World War II. That is either true or false, what I just said.

It is simply not fair to put these provisions which disproportionately benefit business on a credit card. To do so would be incredibly hypocritical, especially since our Speaker has ruled out a vote on the fully paid for extension of the unemployment insurance.

Tax cuts do not pay for themselves. We learned our lesson, I think, in 2001 and in 2003, when the Clinton surplus evaporated and paved the way for structural deficits we continue to see.

We are pleased when the draft of the Chairman's tax reform legislation used the current law baseline. That meant a big deal.

Mr. Hungerford, it is good to see you again. You spent a long time with the Congressional Research Service, and your astute analysis informed many debates in this Committee and throughout Congress.

One report of yours that I almost carry with me all the time, that sticks in my mind, "Taxes and the Economy, an Economic Analysis of the Top Tax Rates Since 1945." I thought it was on target. I have referred to this before in discussing tax issues.

My friends on the other side of the aisle often claim that tax cuts at the top are the key to unleashing economic growth in this country.

Could you please summarize what the research you conducted for the paper I just cited found regarding the correlation between the top marginal and capital tax rates and economic growth and income distribution?

*Mr. Hungerford. To briefly summarize, I found no correlation between changes in the top tax rates for capital gains and for ordinary income and for various measures of economic growth per capita, GDP growth, productivity growth, changes in savings and investment.

I think if there were something there, I would have found a correlation. I think it is very telling that I did not find a correlation. You just do not see any movement, these variables moving together in the data.

I did, however, find as the top tax rates for ordinary income and capital gains have come down, income inequality has been going up, as measured by the share of total income going to the top one percent in the income distribution.

*Mr. Pascrell. We have to get beyond the first flush that would indicate that the more investment that comes from the top necessarily and the more tax breaks the top five percent receive, it is going to automatically transfer into economic growth and jobs in the economy.

You made that study from 1945 on. Why are we still relying on that myth that if we take care of the top, and I am exaggerating, let me use hyperbole, I have that option right now, if we continue to do things for the top, everybody else is going to be wonderful. Why are we still using that myth?

*Mr. Hungerford. I wish I knew.

*Chairman Camp. Time has expired.

*Mr. Pascrell. Thank you, Mr. Chairman.

*Chairman Camp. Thank you. We will go to Mr. Smith.

*Mr. Smith. Thank you, Mr. Chairman, and thank you to our panelists here today for sharing your insight and expertise.

I think you have all touched on the fact that a permanent Tax Code is a somewhat simpler Tax Code. Certainly, it eliminates one of those unpredictable provisions of the Tax Code.

We know that the marketplace is volatile, it impacts the economy in various ways, and Mr. Stallman, I know agriculture certainly sees the volatility in the marketplace and tries to manage that. We hope we do not have volatile tax policy as well.

Especially in light of the fact that I think agriculture has done very well with producing more and using less water, less resources, less land. I think there is a great story to tell there.

Can you perhaps illustrate kind of the added risk to agriculture given uncertain tax policy?

*Mr. Stallman. It impedes the progress of the industry with uncertain tax policy. The risk is without knowing what the tax policy is, without being able to make business decisions, where we have some certainty for the future, then that inhibits us from creating a productive and efficient platform as the industry needs for the future.

You mentioned some of the progress we have made. We have made tremendous progress on so many fronts on productivity but also in use of resources, but a great deal of that has to do with acquiring the technology, the equipment, the tools, to be able to do that. Those are getting more expensive by the year.

Particularly in things like our expensing policy with Section 179, that directly relates to our ability to make those decisions, to maintain an ever improving production platform for U.S. agriculture. Without that, we do not have that certainty and will be inhibited in making those decisions.

*Mr. Smith. More specifically perhaps, could you elaborate in terms of Schedule F filing, what that means to your members and especially how that would relate to permanent tax policy?

*Mr. Stallman. As farmers and ranchers, we do file on a separate schedule, Schedule F, as you referenced. The big issue there for us is cash accounting versus accrual accounting, I think, in terms of being able to file on a Schedule F and being able to frankly manage our finances, our incomes, and our tax expenditures to a certain extent using cash accounting as opposed to accrual accounting.

In the long run, all it does is allow us to sort of remove the up's and down's that are inherent in the volatility that we experience, both in terms of the marketplace and in terms of the weather.

For some years, we will have a very large income. For other years, we will have much less. Without some ability to sort of manage those swings from a tax and economic standpoint, once again, it makes it more difficult for us to do our business as farmers and ranchers.

*Mr. Smith. Thank you again to our panelists, and thank you, Mr. Chairman. I yield back.

*Chairman Camp. Thank you. Mr. Paulsen?

*Mr. Paulsen. Thank you, Mr. Chairman. Mr. Chairman, before I begin my questions, I just want to take a moment to thank you and your attention on this issue for permanency in the Tax Code, but also for the attention you have given in your tax draft to the medical device tax repeal. There are not many such as yourself that paid such close attention to a very unjustifiable tax that is killing good domestic jobs and manufacturing jobs and cutting research and development and denying patients access to those innovative therapies that I think are so critical to our country.

*Chairman Camp. Thank you.

*Mr. Paulsen. Let me ask you this, this is a very helpful exercise. I appreciate your being here today.

As we focus on a pro-growth Tax Code, I think this has been one of the biggest criticisms of Congress, and you really laid out individually on various different aspects of the Code short term fixes versus long term thinking, right?

What should be the direction to go? You can apply that to transportation, health care, and certainly the tax policies as we try to get the economy going.

I hear constantly from companies in particular that say look, if you have a retroactive tax provision, if you extend something for six months, if you extend it for a year, you are not going to have any confidence, certainty or predictability of how we are going to invest capital in our economy. That is why this is a very helpful exercise.

Mr. Redpath, I want to ask you a question. You testified earlier, particularly your comments supporting the extension of this five year built in gains holding period. I am pleased that the Chairman also recognized this is a very important provision and it is included in the tax reform discussion draft.

This might seem like a subject that is very trivial, and accountants such as yourself are aware of it, it might not have an actual impact on our economy on a grand scale, but IRS statistics do suggest that thousands of U.S. businesses, thousands of U.S. businesses are actually sitting on top of appreciative assets that could be put to better use.

You gave a couple of examples of that. In an economy that is short of capital now, it just seems to make sense to me that we allow businesses increased access to their own capital, their own assets.

You mentioned in your testimony the lock up or lock down of that capital that the built in gains taxes result in. How difficult has that issue been for S corporation clients that you work with?

*Mr. Redpath. It has been difficult. Let me talk about that. I am a tax accountant. I thought it would be my responsibility to remind all of you that your returns or extensions are due next Tuesday.

[Laughter.]

*Mr. Redpath. We have clients that look at how they can raise capital. When their capital is locked up as a result of this provision, what can they do. One thing you have to remember is S corporations cannot get money from the public markets. Public companies cannot be S corporations.

What are their alternatives? One is they can go borrow money. Most small businesses are not interested in borrowing large chunks of money to raise capital. They can consider selling part of their shares to venture capitalists or private equity firms who have probably competing interests and conflicting interests with regard to ownership. Generally, they are looking at flipping a company.

Most of these companies I am talking about are closely held family businesses. You know how they generate capital? The old fashioned way, they earn it. They make money. They pay their tax. They retain it.

What causes them to slow that down are a few things. Tax rates. Tax rates matter to flow through entities. In Minnesota right now, many flow through entities are paying in excess of 52 percent combined Federal and state taxes. That is after paying sales tax, property tax, excise tax, payroll taxes, and the built in gains tax.

They are sitting on capital like we talked about, that they cannot generate the old fashioned way by earning it and converting it to the appropriate assets to increase earnings. Truly, the small businesses I work with, that is their primary way of generating capital, through earnings.

*Mr. Paulsen. Actually, a little esoteric provision of the Tax Code that is dealt with from a permanency perspective can actually drive a lot of economic growth, can be a pro-growth initiative, you are saying, and there are other avenues that some of these S corporations or closely held family businesses might have to access capital, but they are not easy to access.

*Mr. Redpath. They are not easy to access and they do not serve the purpose of the entity, the business, and the stakeholders of the business; no.

*Mr. Paulsen. Thank you, Mr. Chairman.

*Chairman Camp. Thank you. Mr. Davis?

*Mr. Davis. Thank you very much, Mr. Chairman. I want to thank you for the hearing, and I want to thank all of our witnesses for coming, especially I want to welcome Ms. Zelisko from Lake Forest, Illinois, just a few miles from my District and from Chicago.

Mr. Chairman, while I am pleased we are considering these seven areas, I would look forward also to looking at transit parking and things like low income tax credits, new markets tax initiatives, work opportunity tax, tuition credits.

I have two documents I would like to submit for the record from the Regional Transit Authority and from the National Growers Association. I ask unanimous consent.

*Chairman Camp. Without objection.

*Mr. Davis. Thank you very much, Mr. Chairman.

Ms. Zelisko, let me ask you, the research tax credit has been vital to ensuring that the U.S. is in the best place in the world for companies to conduct research and business.

I know you work for one of these companies and work with companies. Could you tell us how your company has made use of this area?

*Ms. Zelisko. The research and development credit?

*Mr. Davis. Yes.

*Ms. Zelisko. Yes, it is very important to the company. It is an important element of determining what projects we are going to be looking at because it determines our cash flow.

We obviously generate cash flow from our earnings in the company, but that cash flow is increased by the research and development credit because it does reduce our tax liability, and that money is then redeployed into investing in new products for the consumer, meeting environmental requirements about emissions.

These are all important items that therefore generate jobs, and with the successful product that I mentioned, about a 150 horsepower four stroke marine engine, so successful we had to expand our plant, therefore, that means brick and mortar that were added, and created jobs in the construction business, and also created additional jobs for engineers that we have in Fond du Lac, Wisconsin.

This plus in our marine business with regard to the different items that I listed in my written testimony, all the different products and innovations we have made, given the competitive nature of the business in which we do business.

*Mr. Davis. Thank you very much. Mr. Hungerford, you discuss in your testimony the reasons why it is important to be fiscally responsible when addressing tax extenders.

What would be the likely effect on the GDP and economic growth if the seven provisions discussed today are made permanent without paying for them?

*Mr. Hungerford. Just comparing to the baseline, I would expect that GDP growth going out would be smaller or would be lower. If interest rates do go up, we will end up seeing less investment, which will have an impact on GDP growth, on jobs, and employment possibilities.

*Mr. Davis. Thank you. Mr. Stallman, would you briefly tell us how Section 179 expensing rules are used in the farming industry?

*Mr. Stallman. Let me just illustrate that with an example. For instance, if I need to go out and buy the tractor I referenced, let's just say it costs $200,000. Without Section 179 expensing, I would be limited to taking the deduction, and let's assume it is used and not new, I would be limited to taking a deduction of $25,000 and then depreciating that over multiple years.

That affects my cash flow. Therefore, I would have to not have the benefit of postponing some tax payments, if you will, by accelerating the depreciation, and then having to take those expenses in future years, so the net effect roughly would be the same over time, but the point is that extra cash flow that would be allowed by being able to accelerate the deduction used in Section 179 expensing would allow me to more easily make the investment.

*Mr. Davis. It becomes very helpful in making sure that you would be able to acquire and make use of that John Deere?

*Mr. Stallman. Absolutely, except mine is Case IH, Congressman.

*Chairman Camp. All right. Thank you. Mr. Reed?

*Mr. Reed. Thank you, Mr. Chairman. I just wanted to explore, Mr. Odintz, if I could, as I co-chair the U.S. Manufacturing Caucus also down here in Washington, D.C., and focusing on AFE, the active financing exception, can you give a little detail, more analysis, as to how U.S. manufacturers can become more competitive by the AFE exception and how that impacts U.S. manufacturers' ability on a competitive basis internationally?

*Mr. Odintz. Sure. An U.S. manufacturer when it decides to export goods manufactured in the United States abroad can establish under AFE a financing or leasing subsidiary in a foreign country. That leasing subsidiary or financing subsidiary can offer financing on expensive widgets, like earth moving equipment or very expensive other equipment, airplanes, et cetera.

What it allows that company to do is to compete on a financing perspective, provide similar terms as foreign competitors.

Let's say a widget maker based in the United States sells its product in the European Union. A similar company making a similar widget based abroad is going to offer financing terms that are reflected in that market, and what the AFE does is it allows the U.S. manufacturer to provide the financing terms that are equivalent, that can be provided by other foreign financial institutions.

*Mr. Reed. Do you have any analysis or any data that you could support that if AFE was not extended on a permanent basis, it would put U.S. manufacturers at a competitive disadvantage?

*Mr. Odintz. I do not have macro data. I can see from clients that their terms of leasing or loans may be higher than competitors, which puts U.S. manufactured goods at a competitive disadvantage.

*Mr. Reed. Does anyone else on the panel have any data or impacts from any of their clients or anything?

[No response.]

*Mr. Reed. I also wanted to explore a little bit the look-through issue. The temporary nature of the rule -- obviously, being a country lawyer from Western New York, small business owner, one of the biggest things, and we have already heard it numerous times here today, is the lack of certainty really impacts the ability to plan.

I always had a business plan. I had a five year plan, ten year plan, and I did that with 30 employees that worked in our businesses that we created.

If you do not have that certainty, tell me from the look-through perspective, what kind of decisions -- nuts and bolts -- what kind of decisions are put off, which ones are prevented or which ones are not taken as a result of having that lack of certainty?

*Mr. Odintz. Sure. For example, clients that do not have look-through have to price in the cost of capital and whether and where to expand foreign operations.

Obviously, if the company has to take loans from banks, that cost of capital is more expensive rather than deploying its own internal capital from one jurisdiction to another.

When a company determines whether and where to expand its operations, it takes into account the after tax profit, and then it is interested in making an after tax profit. Not having CFC look-through adds to that cost of capital and makes it more challenging to expand foreign operations.

*Mr. Reed. Does anybody have any anecdotal kind of cases you could share with the Committee as to actual jobs and expansion here on American soil that was caused because of this lack of certainty?

*Mr. Odintz. Obviously, it is also important to have permanence or at least more than an one year extension because business decisions are not made on an one year basis. They are long term. Businesses want to derive profits over the long term and make permanent decisions. A temporary provision makes it difficult to plan for the long term.

*Mr. Reed. That is a great point. We are talking about large capital investments here. What would be the size of the typical investment we are talking about?

*Mr. Odintz. For example, building a plant is a rather expensive endeavor. It requires also hiring a labor force to build that plant. You are looking at multiple billion dollar investments in many instances.

*Mr. Reed. If you do not have that certainty to make that decision on that multimillion dollar decision, that is what you are referring to, that is where the rubber meets the road, so to speak.

*Mr. Odintz. Exactly.

*Mr. Reed. With that, Mr. Chairman, I yield back.

*Chairman Camp. Thank you. Mr. Young?

*Mr. Young. Thank you, Mr. Chairman. Thank you to all of our panelists for testifying here today, really appreciate all we have learned.

I want to thank the Chairman in particular for making permanent the CFC look-through provision in the draft and holding a hearing so we might discuss that provision in particular a bit further.

I have concerns about our intellectual property intensive related firms and also our continued investment in R&D, which as we all know is essential in this modern economy we live in.

I look forward to working not only with all the members of the Ways and Means Committee on that but other stakeholders as we try to improve the international sections of the draft.

As sort of a lead in to R&D, Ms. Zelisko, you indicated something that many of us have read and I think many of my constituents intuitively understand, which is the U.S. does not have a monopoly any more on global R&D. In fact, you cite a figure, since 2001, the share of the world's R&D performed in the U.S. has decreased from 37 to 30 percent, and to the extent we could arrest that trend line, that would be a good thing, I think we would all agree.

Can you talk about what role tax policy plays with respect to that dynamic?

*Ms. Zelisko. Companies look at the world on a global basis. We are no longer international. We are global businesses. Therefore, looking to where you are going to deploy your R&D is important, and therefore, the impact of tax policy plays a part and is a factor.

This is an opportunity for the U.S. to lead as far as where do we want the technology. Do we want it here, do we want it outside the United States. I think we want it here. It provides jobs. It provides innovation, technology, and from that technology, spurs other technologies.

I think good tax policy is going to look at broad based simplified, something that is administrable. I think the alternative simplified credit provides that.

I would encourage that it be increased to 20 percent, as far as being truly an incentive, and also broad based on the qualified research expenditures that would qualify for the record, I think is important.

When you look around the world, they are not reducing the expenditures. They are increasing them or they are increasing the amount of the credit or the multiplicand on the deductibility of the particular expenditure.

I think good policy would be broad based with regard to what would qualify for qualified research expenditures and the actual amount of the incentive.

*Mr. Young. It needs to be in short made more inclusive, more generous, from your vantage point, but you certainly support the permanency of the provision?

*Ms. Zelisko. Absolutely. That is critical. I think that is sort of like a baseline, you need to have permanency. When we are making business decisions, especially in the R&D area, you are looking out, like I mentioned, four to five years, so you need certainty with regard to it is going to be there during the entire process.

*Mr. Young. Thank you. I represent a District in South Central Indiana, Southern Indiana, and it is very diverse economically. We have a fair amount of small and medium sized manufacturing, certainly IP rich firms, both in the District and around the District, and also agriculture plays a significant part in our economy.

Mr. Stallman, pivoting to the ag sector, you described the Farm Bureau's perspective related to the impact of the $250,000 Section 179 threshold versus a $500,000 threshold.

Why is the higher level so important to your members? It pertains to just the ability to buy more farm equipment, you need a more generous level to incentivize them to do so?

*Mr. Stallman. Yes, the difference, and I tried to convey that in my oral statement, the difference between the $500,000 and the $250,000. It is primarily related to what we are seeing in the cost of the equipment and capital expenditures we have to make in agriculture. It is continuing to increase very rapidly.

Frankly, while $250,000, ten years ago, you could buy you a lot of equipment. Not so much any more. That is why the $500,000 is very important.

*Mr. Young. The inflation of those costs is certainly something we need to take into account, balance that against the lower 25 percent rate, and I guess every individual farm is going to have to come up, individual operation, with the sort of net impact.

Does the Farm Bureau have a policy articulated with respect to that tradeoff?

*Mr. Stallman. No, we do not. We are looking at the whole draft proposal to see where those tradeoff's are. It would vary tremendously across individual operations.

As a general rule, that expensing provision, I think, would probably have more positive impact on farms and ranches in the way they make their decisions, even though it is not tax avoidance because you are just postponing paying the taxes, than perhaps lower rates. Once again, it would depend on the rates.

*Mr. Young. Thank you.

*Chairman Camp. Thank you. Mr. McDermott?

*Mr. McDermott. Thank you, Mr. Chairman.

Ms. Zelisko, Mr. Young and Mr. Reed have sort of laid out sort of what I was thinking about, which is I was a Ways and Means Chairman a long time ago in a state legislature where a businessman told me I do not care what rate you charge me, just tell me what it is, how long it is going to last, so I can figure out how to amortize it. That is really what you are saying about the planning.

The Chairman has one other power, and that is to set the agenda. Today, we are discussing seven tax provisions. There are a whole lot of them that have not been discussed. I think some of the ones that are up here are sound.

I think the research and development tax credit is good policy. Even if the draft probably needs a little revision, specifically in the area of software -- I think Mr. Young already mentioned that some of us who come from areas like I do where research is a big issue and software, we would like a little tweak or two on that whole provision.

The real question is about the ones that are not going on, and why are we not debating them. Residents in states with an income tax can deduct their income taxes. Residents in states that have a sales tax in lieu of an income tax cannot deduct their sales taxes if we do not pass the extender in this bill.

You have to ask yourself what the impact of that is going to be. I would suggest in Washington State, Florida, South Dakota, Wyoming, Alaska, Texas, the Republicans are raising taxes on consumers, those of us who are claimants on a sales tax in the State of Washington will pay $2,000 more in taxes next year if we do not have that extender.

I have to ask myself what kind of impact that would have, and I think Mr. Hungerford, maybe you have an idea, if we raise taxes on people at the consumer level but not extending the sales tax exemption, what is the impact of that?

*Mr. Hungerford. In the short run, it does take money out of people's pockets that they would ordinarily spend. I guess the question is who actually takes the deduction for state and local sales taxes, how much you save and how much you spend of your income depends on where you are in the income distribution.

Without actually looking at the data, it would be hard to say what would be the actual economic impact but to the extent the money that ends up going to the Government, if it had been spent, it would have at least provided some short term stimulus to the economy.

*Mr. McDermott. This is free money we are talking about here today. We do not have to pay for this. Would it be better to give money to the consumers to spend in the economy than to give money to companies to do research? How do you make that decision?

*Mr. Hungerford. It is a tough decision to make.

*Mr. McDermott. We are not having a discussion about the whole broad range of extenders. We only have these seven over here, so they were selected by somebody to be exactly what we ought to be doing.

I also have one I have some question about, what the point of it is. Why under the Chairman's plan -- what makes sense to make charitable deductions only if the contribution exceeds two percent of the individual's adjusted gross income.

It sounds like we are putting a floor in there, and the CBO said imposing a floor would lower contributions. Why do we want to lower contributions by putting a floor in?

What would be the advantage to society at a time when we are looking for people to give money to whatever? How is that better for society?

*Mr. Hungerford. Actually, I have not looked at CBO's study on how much it would lower contributions. On the margin, it would not have any effect, just because the people who are on the margin would be above, well above that two percent of the AGI threshold.

Of course, it would not affect people who do not itemize, many people make charitable contributions and are not allowed to take a deduction because they do not itemize. Then there is this group in there, I do not know to what extent they would be affected. I would expect there would be some effect. I am just not sure how large it would be.

*Chairman Camp. All right. Thank you. I would just say this is a first in a series of hearings. These items were chosen because they are in the discussion draft. We wanted to start with these.

As you know, the President's budget has proposed a ceiling on charitable contributions, which in our hearings, the charitable community has very much opposed.

Obviously, in order to lower rates as we do in the draft, there are tradeoff's. The analysis is that charitable contributions will actually increase by $2 billion a year because of a lot of the moving pieces in the draft, not just this provision looked at in isolation.

*Mr. McDermott. Would it be your intention that when we have a mark-up, we would have the ability to offer other amendments than the seven that are in your bill?

*Chairman Camp. Yes. We are going to have hearings on a series -- I am not exactly sure of the procedure we are going to take in terms of a mark-up yet -- there will be probably more than one mark-up going forward.

*Mr. McDermott. More than one mark-up.

*Chairman Camp. Probably more than one mark-up going forward. I have not fully decided that yet.

*Mr. McDermott. I just want to reserve the right to offer an amendment at some point on the sales tax in Washington State, in Texas and in Florida.

*Chairman Camp. I understand your interest there.

We are now at Mr. Kelly.

*Mr. Kelly. Thank you, Mr. Chairman. Thank you for having this hearing. Thank you all for being here.

I come from the private sector. When we talk about taxes and what we are trying to do, pro-growth tax reform could probably not be more important than anything else we do in this country other than also regulation reform.

I am more interested in people that come from the private sector because they are the ones that provide all the revenue that is needed to run all these wonderful, wonderful programs we have.

Mr. Stallman, you are in agriculture. You made a statement, the ability to have some type of predictability or certainty is absolutely critical to any of us in the private sector. There is an old saying out there, if you do not know where you are going, any road will get you there.

At this point right now, what the Chairman has offered is a road, a path to prosperity, part of it being this tax reform. I think sometimes people get mixed up. I hear all these different talks about this section, that section, every little section. People will sit down and debate that for hours.

At the end of the day, the question becomes are we helping to grow this economy or are we making it tougher for people who actually supply the revenue to get there. We are making it so hard on the private sector to get there, and then holding them accountable for not supplying enough revenue.

The last time I looked, the only people paying taxes are working folks and companies that are profitable. This tax reform is absolutely critical right now.

Mr. Stallman, you started to talk about making capital investments. There is no way in the private sector if you do not know the certainty of where this Tax Code is going to be that you can make a long range commitment to do something. You just cannot do it.

Each of you, I would like you to just weigh in a little bit, because it is really important, not so much for us here in Congress, but for people back home to understand what it is like.

They have got up every morning and swung their feet over the side of the bed and went to perform some type of an activity that will support their families, support their communities, support their region and their country.

This thing has gotten so far out of control. You all know this. The cost of tax preparation, not the tax bill, preparation, $168 billion, in about seven billion hours. My goodness. Could that time have been spent a little better and could that money have been reinvested?

I am looking at capital investments. You have to have some reason to do that. We are truly engaged right now in a global economy; right? We just do not compete -- Illinois does not just compete with Ohio. Pennsylvania does not compete with New York. We compete with everybody in the world.

The last time I looked, we had the highest taxes in the world. Is that right? Any of you in the private sector, please tell me, part of your economic model is total cost of everything you do, which includes tax obligations, is there anything about what we are trying to get to that does not make sense?

The Chairman just said today we are only talking about some of the extenders. What can we do? What can we do to give all of you in the private sector a little look in to the future, you know what, they know where they are going and they are going to make it easier for us to get there?

I hate like heck the fact that we seem to be adversaries of yours and not advocates, and then we turn around and hold you responsible for not supplying the revenue that we think is necessary for all these wonderful programs.

Any of you that want to weigh in on that, America needs to hear that we get it, we understand their plight. This is to any of you.

*Ms. Zelisko. I would like to offer that I do not want the U.S. to be 22nd in the world as far as research and development incentives. I want us to be number one.

A way to get there is obviously making the credit permanent, broadening what is included in those qualified research expenditures, including what we currently have of supplies and software expenditures, along with the wages from the engineers and scientific individuals that we employ to provide that improved technology.

When you are an innovator, lots of things sprawl from that. I think if the policy is set, that we have the certainty, companies will become once again a source of tremendous innovation here in this country.

*Mr. Stallman. U.S. agriculture is the number one exporter in the world. We have built a very strong, productive, efficient, competitive industry in this country, and we want to keep it. I think that is the crux of the issue.

What do we need to keep it. We need some certainty around tax policy. There is a sense, I believe, in the countryside, that farmers wake up one day in the Spring and say, oh, golly gee, I have to go out and plant something. The reality is they are making plans three, five, and ten years in advance in terms of their capital expenditures, how they manage the infrastructure of their farm and ranch, and how they are going to be even more productive in the future.

Having uncertain tax policy laid over that, it makes that task very difficult, to plan for the future and continue to be competitive and efficient

*Chairman Camp. All right. Thank you. Mr. Marchant?

*Mr. Marchant. Thank you, Mr. Chairman. Thanks for bringing forth what are the most important extenders as far as my District is concerned. The modified research credit made permanent would have a very significant impact in my District.

I have a District that has the headquarters of Exxon, Fluor, Kimberly-Clark, AT&T, and Verizon. All of those companies rely very heavily on the research and development, but really the impact of these extenders that we are talking about today and their correlation to the long term tax reform really hits home in those thousands of businesses that surround these big companies.

My District surrounds the DFW Airport. I literally have thousands of businesses that rely very heavily on Code Section 179.

As we speak, there are people sitting in their offices with their accountants, because this is the week they are talking to them, and they are talking to them about should I buy and can I buy a new truck, should I buy a new machine, how about a new forklift, how is that going to affect me.

They are talking at this moment about well, we do not know whether Section 179 of the Code is going to be extended. If you buy the truck or you buy the forklift or you expand your business at this point and they do not extend it, here is going to be the tax treatment, here is the implication it is going to have on your business, but if they do, this is what is going to happen.

Mr. Hungerford, what kind of impact would that have not on future economies but just the recovery that we are experiencing now, the slowness of our recovery? What kind of impact will that begin to have in the coming months on businesses, their expansion, the auto industry, the tractor industry, et cetera?

*Mr. Hungerford. My guess is not a great deal, I have always found that temporary tax provisions that are designed to stimulate the economy rarely stimulate the economy.

*Mr. Marchant. You would consider this just to be a temporary tax stimulation and should not be included as part of this --

*Mr. Hungerford. Section 179 expensing?

*Mr. Marchant. Yes.

*Mr. Hungerford. The thing is if you let it expire now, or actually it is already expired, and fail to extend it, I do not think it will have a large impact on the economy.

*Mr. Marchant. Is there any disagreement among the panelists on that?

*Mr. Stallman. I do not have a study to back it up. All I know is the behavior of farmers and ranchers. I will tell you that with the certainty, with Section 179, they will be more inclined to accelerate their capital acquisitions than what they would otherwise, and be more capable of doing it because of cash flow benefits that occur up front.

Long term, once again, they are going to be having less expense in the future to deduct, but that behavior will create more economic activity. I do not know about what the impact would be.

*Mr. Marchant. Mr. Redpath?

*Mr. Redpath. My clients are interested in planning. If the law is permanent, it is much easier to plan. Lots of my clients are now holding off on making acquisitions because they do not know what the rules are. I believe that is going to have a snowball effect on investment and on the other larger companies around that are impacted by these small companies working with them.

*Mr. Marchant. Thank you, Mr. Chairman. I yield back.

*Chairman Camp. Thank you. Mr. Griffin? Last but not least.

*Mr. Griffin. Thank you, Mr. Chairman. I know a lot of the questions I might have wanted to ask have been covered, so I just want to make a few comments.

I have heard the uncertainty argument ever since I first ran for Congress and totally agree with it. I hear it regarding the Tax Code. I will be real honest with you, from a lot of people I hear it regarding this Administration, they are waiting until this Administration is gone before they invest because they believe it is an anti-business, anti-growth Administration.

Let me say this. I want to applaud the Chairman for tackling tax reform. I know not everybody likes 100 percent of it. You are never going to find that in Congress. I think it is a historic moment to start that conversation.

We do need to get away for the sake of certainty from a lot of the patches, whether it be in SGR, Medicare, or on our Tax Code, or whatever else. We need that certainty that you are talking about. I believe our growth is tied to fixing the Tax Code in large part.

I did my own taxes this past weekend, finished them. They are relatively simple in terms of complexity, but it was ridiculous how much time it took me.

I am embarrassed for the country, to be frank, at the complicated nature of our Tax Code. I can see with me, an individual, how complicated it is, and it pains me to think of what you guys have to go through. I appreciate your being here.

Until we do get it fixed, I also applaud the Chairman for taking the steps necessary to address these issues. I am a firm believer in R&D. I will tell you I do not want to just beat other countries, I want to beat them so badly that companies around the world say there is only one place in the world to do business, and that is the United States, and there are no other options.

I can tell you that is not the state of affairs right now. I think the Tax Code is part of it. Certainly, we need to encourage R&D.

I would just point out that I have a lot of agriculture not only in my District but throughout Arkansas, and the small business expensing is critically important to them and many others.

Such is the burden of being last in line, all the good questions are gone. I want to just thank you for being here and thank you for what you do, and I just want to say thank you to the Chairman for putting these issues on the table and for starting the discussion about what we can do.

The one thing we can agree on is the status quo is unacceptable, and we can do much, much better than we are doing.

Thank you all for being here.

*Chairman Camp. All right. Thank you. Thank you all very much, very much appreciate your testimony this morning, and with that, this hearing is adjourned.

[Whereupon, at 12:17 p.m., the Committee was adjourned.]

Public Submissions for the Record

American Association of Fundraising Professionals

Beau Pollock

Brunswick Corporation

Building Owners and Managers Association International

Cambridge Engineering, Inc.

Concord Engineering

Dickman Industrial & Electrical Supplies

Edgewood Green Technologies

Finegold Alexander and Associates Inc.

Lane Associates

Lawrence Steiner

Matt Henry

Mechanical Service & Systems

National Affordable Housing Management Association

National Education Foundation

National Grocers Association

National Restaurant Association

Peter M. Honeyford

R&D Credit Coalition

Radian

Regency Lighting

Solid State Capital Services

The American Institute of Architects

The Apple Gold Group

The National Treasury Employees Union

True Partners Consulting, LLC

TrueBlue, Inc.

Vikki Spruill

WageWorks

Walker Parking Consultants