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Committee on Finance
"American Made: Growing U.S. Manufacturing Through the Tax Code"
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Chairman Wyden, Ranking Member Crapo and distinguished members of the committee, thank you for holding today's important hearing focused on how the U.S. tax code impacts manufacturing in America.

My name is Courtney Silver, and I am president and owner of Ketchie Inc. located in Concord, North Carolina. Ketchie is a third-generation, full-service precision machine shop that was established in 1947. Our mission is to support the entire U.S. manufacturing supply chain by delivering competitively priced, high-quality machined parts on time. We invest in machining equipment and technology, people and processes to make it easy for our customers to focus on what they do best and to have confidence in their supply chain.

My testimony will focus around one main theme today, and I hope if members take away anything from me, it is this: **Manufacturing is a team sport.**

Like any great sports franchise, a team can only excel if every player is operating at their peak. If not, the team falls apart. Similarly, the manufacturing supply chain is only as strong as its weakest link. At the core of any sport are clear, sensible rules that don't unfairly handicap any players in the game. These rules are consistent, rather than constantly changing, so that the game does not devolve into chaos. In this context, the rules of the game are the U.S. tax code. Our tax code needs to be simple, consistent and pro-growth so that it supports manufacturing and gives us all a chance to compete to our fullest potential.

The 2017 Tax Cuts and Jobs Act was revolutionary for the manufacturing sector. After the legislation was signed into law, Ketchie experienced the best year in our seven-decade history. I know others further up our supply chain were booming as well, because I can clearly remember our typically organized shop floor covered in pallets of materials in every available space to keep up with orders. My customers were able to plan facility expansions, introduce new product lines, invest in R&D and enter into long-term stocking agreements with Ketchie due to this industry boom. This was great for us, too: our sales revenue increased 25% in that first year.

As a result, in 2018, we were able to invest more than $1 million into capital equipment, which helped us meet the surge of demand as our customers ramped up production. We expanded our shop floor workforce by 20%, developing our team at Ketchie to keep pace with the ever-evolving manufacturing industry.

When you want to succeed, the only choice is to use your profits productively and pour them back into your team. We made major investments in capital, such as new machining equipment and technology, advanced robotics, tooling, fixtures, HVAC systems for our facilities and new security and safety systems for our team members. We were able to provide 100% of our team members, no matter how long they had been with the company, with pay raises and quarterly bonuses. We expanded our team members' benefits, including enhanced 401(k) matching. I was excited to see that because of these choices, our dedicated team members were buying their families their first homes and first cars. Ketchie was also able to do more to support our community, grow our charitable giving and take on more volunteer opportunities.

Ketchie has made a commitment to focus our resources on bringing up the next generation of manufacturers. In 2023, I created "Opportunity Knocks," an internship program for high school students that allows them to shadow experienced machinists in our factory while earning school credit. The local high school we partnered with consists of 70% minority students, and almost 100% come from economically disadvantaged situations. I would not have been able to establish this program or invest in the machinery and the team members necessary to make it a success without the TCJA. Because we have been able to expand and invest in exciting technologies, students are learning valuable trade skills while also preparing for careers that will bring them fulfillment and pride.

Members of this committee must understand that small and medium-sized manufacturers operate on extremely slim profit margins, so all of these changes—higher wages, investments, increased charitable giving—were thanks to these pro-growth tax reforms.

Of course, our growth trajectory was disrupted during the COVID-19 pandemic like the rest of the world. However, thanks to the TCJA policies having such an impact on Ketchie in 2018 and 2019, we were able to withstand the shutdowns and supply chain disruptions, even as some of our customers went out of business or were unable to pay tens of thousands of dollars in open invoices for the better part of 2020. This would not have been possible—and Ketchie might not be here today—if we didn't have an economic boom in the years prior to the pandemic.

Small manufacturers across the country realize how significant the job was for Congress to advance generational tax reform in 2017. The alterations made to our tax code allowed a small manufacturer like me to play on a global scale by making it an easier call for my customers to invest their dollars here rather than in a competitor overseas. Manufacturers are facing stiff competition around the globe from countries enticing companies to bring their business out of the United States. A strong domestic manufacturing sector directly correlates to increased national security and economic prosperity for all Americans.

Beginning in 2022, the rules of the game began to change making it much more difficult for manufacturers to thrive in America. Crucial policies enacted by the TCJA began expiring or phasing out, including the ability to immediately deduct research and development expenses, enhanced interest deductibility on business loans and the ability to deduct the cost of capital investments in the year acquired. These provisions, along with many others in the TCJA, gave us the confidence and stability we needed to invest and grow our operations. Manufacturers rely on stability from our tax code for assurance that we can make decisions in the short term, but also plan ahead and make investments that will pay off for decades to come.

Congress enacting pro-growth and permanent tax policies allows us to do all of this and so much more.

A. The Tax Code Must Promote Certainty for Manufacturers

It is imperative that this committee recognizes the fact that all domestic businesses rely on predictability and stability within the tax code. Ketchie's experience with the benefits of tax reform was not an outlier. Following TCJA passage, the manufacturing sector experienced the best year for manufacturing job creation in the previous 21 years and the best year for manufacturing wage growth in the previous 15 years.[1] Manufacturing capital spending grew 4.5% and 5.7% in 2018 and 2019, respectively.[2]

Yet today, due to the uncertainty that Congress will address the expiration of federal tax incentives related to R&D, interest deductibility and expensing for capital investments, 40% of manufacturers said they have already been forced to pull back on hiring and investing.[3] In the same survey, 94% of manufacturers said that it is important for the federal tax code to help reduce manufacturers' costs for conducting R&D, accessing capital via business loans and investing in capital equipment purchases.

Ketchie, like most manufacturers, is a capital-intensive business. In the years following the TCJA, I was able to make a higher level of investment because I knew our tax code was going to have a baseline of certainty. Today, however, I am unable to make these investments because of the uncertainty that Congress will address the expired TCJA provisions. This is not unique to Ketchie; I see my customers and fellow local manufacturers being forced to pull back on expansions or hiring opportunities due to the uncertainty.

I receive a daily reminder of this when I walk on my shop floor. I have a very large space on my floor reserved for my next significant machinery investment. This investment will allow Ketchie to operate in new industry markets, and to inspire and attract the next generation of top talent who want to work with the most cutting-edge technology possible.

This investment is *on hold* due to the phasing out of the accelerated depreciation levels from 100% in 2022 to 60% in 2024. Because I am unable to realize the full deduction of my investment within the year I purchase it, the investment seems too risky and irresponsible. Permanent full expensing allows me to invest, grow, compete and create highly skilled and high-paying jobs. These positions give people dignity and purpose and change their lives in our community. If accelerated depreciation is allowed to expire fully in 2027, I truly don't know how we will be able to purchase the equipment we need to continue to expand our business.

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[1] National Association of Manufacturers, "Competing to Win" (September 2022), *Available at* https://documents.nam.org/ctw22/competing%20to%20win%202022%20-%20tax.pdf.
[2] Id.
[3] NAM Manufacturers' Outlook Survey, First Quarter 2024 (March 5, 2024), *Available at* https://nam.org/wp-content/uploads/2024/03/Outlook-Survey-March-2024-Q1.pdf.

According to the Joint Committee on Taxation,[4] the manufacturing sector, and specifically small manufacturers, overwhelmingly utilize accelerated depreciation more than any other sector. I would like to thank Sen. James Lankford and many members on this committee that joined him for introducing the Accelerate Long-Term Investment Growth Now Act, which would make 100% accelerated depreciation permanent. Legislation like this is what allows manufacturers to have tax-planning certainty for the future.

Additionally, at the beginning of 2022, the deduction for interest on business loans was reduced in a manner that disproportionately affects manufacturers. The maximum deduction allowed under Section 163(j) of the tax code was narrowed from 30% of earnings before interest, tax, depreciation and amortization (EBITDA) to 30% of earnings before interest and tax (EBIT). Excluding depreciation and amortization would reduce the amount of interest businesses can deduct, making it more expensive for manufacturers to finance capital equipment purchases.

Because we do not carry as much debt typically, Ketchie may not experience a direct impact of this tax policy change. However, our customers up the supply chain certainly do, which means the impact of this tax policy change makes its way downstream to us. The majority of my customers buy and sell large pieces of capital equipment that require debt financing, and their inability to deduct interest makes borrowing more expensive, threatening Ketchie's economic health and ability to grow.

Allowing this stricter limitation to continue greatly affects manufacturers' ability to compete globally. Among the 35 countries that have a rule that restricts tax deductibility based on a ratio of interest expense to some measure of earnings, the United States is the only country that has an EBIT-based rule. Generally, China does not limit *any* third-party interest deduction. According to a recent study, keeping the EBIT standard could cost the U.S. economy 467,000 jobs and reduce the U.S. GDP by $43.8 billion if Congress does not act.[5]

I would like to thank Sens. Shelley Moore Capito and Kyrsten Sinema for introducing the American Investment in Manufacturing Act, which would reverse this harmful policy that disproportionately impacts manufacturers.

Ketchie delivers machining solutions to government and commercial customers in a wide range of industries, including rail, agriculture, textile, heavy machinery, industrial equipment and many specialized original equipment manufacturers. Our ability to innovate is what keeps us in the game, and a large part of that for the manufacturing sector as a whole has been the ability to deduct R&D expenses.

For decades, taxpayers have been allowed to immediately deduct 100% of their R&D expenses in the year they incurred. In 2022, however, the tax code began requiring so-called "amortization" of these expenses, forcing manufacturers to recover only a small portion of their costs over several years.

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[4] Joint Committee on Taxation, "Tax Incentives for Domestic Manufacturing," JCX-15-21 (March 2021), *Available at* https://www.jct.gov/publications/2021/jcx-15-21/.
[5] "Economic impact of a stricter 163(j) interest expense limitation," EY (September 2022). *Available at* https://documents.nam.org/tax/nam_interest_deductibility_study.pdf.

Taxing manufacturers' investments in critical R&D expenditures means that we will have less funds to invest in workers and our future growth. The private sector accounts for more than 75% of total R&D spending,[6] with small businesses accounting for approximately $90 billion of all private-sector R&D investments.[7] This is not a new issue—the tax code has recognized the importance of R&D spending for more than 70 years, but with this recent change, Congress has now made the U.S. one of the two developed countries in the world who require the amortization of R&D expenses.

A new report from the European Union found that both the EU and China gained a significant advantage after the expiration of the TCJA R&D tax policies.[8] In 2022, the first full year after immediate expensing for R&D expired in the United States, EU R&D growth surpassed the U.S. for the first time in nearly a decade. Even more worrisome, China's R&D growth tripled that of the United States in 2022. Chinese companies enjoy a super-deduction on research spending, while American firms must now compete with weights strapped to their ankles following the expiration at home. China is not the only country offering better R&D incentives—17 countries now provide a deduction that is more than 100% of eligible R&D expenses, further making the United States a less attractive place to conduct R&D.

At Ketchie, we challenge ourselves to provide our customers with a good reason to spend their dollars here. At a time of increasingly fierce global competition for research dollars, Congress must act to ensure the next R&D dollar is spent in the United States to secure our global leadership in innovation and strengthen our nation's economic and national security. I want to thank Sens. Maggie Hassan and Todd Young for introducing the American Innovation and Jobs Act this Congress to support R&D investments by manufacturers.

Finally, our tax code should be simple. As a small manufacturer, hiring outside accountants and lawyers to understand and navigate every piece of the tax code is costly and time consuming for me. Our tax system should not be so complicated that small manufacturers don't even have a chance because we are crushed by red tape and unnecessary bureaucracy. Congress should craft our tax code so that it enhances competitiveness and encourages industrial investment here in the United States.

At the time of this hearing, the Senate has the opportunity to address these three expired tax provisions. On Jan. 31, 2024, the House of Representatives passed the Tax Relief for American Families and Workers Act, which would allow for the TCJA R&D, interest standard and full expensing provisions to be extended from their expiration until 2025. If the Senate fails to renew these business provisions, manufacturers will be playing with one hand tied behind their back for the foreseeable future. I urge every member of this committee to show their support for these business

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[6] National Center for Science and Engineering Statistics, National Science Foundation, National Patterns of R&D Resources: 2020-21 Data Update, NSF 23-321 (Jan. 4, 2023), *Available at* https://ncses.nsf.gov/pubs/nsf23321.
[7] National Center for Science and Engineering Statistics, National Science Foundation, InfoBrief, NSF 22-343 (Oct. 4, 2022), *Available at* https://ncses.nsf.gov/pubs/nsf22343 and InfoBrief, NSF 23-305 (Dec. 14, 2022), *Available at* https://ncses.nsf.gov/pubs/nsf23305.
[8] "EU Industrial R&D Investment Scoreboard" (2023), *Available at* https://op.europa.eu/en/publication-detail/-/publication/1e5c204f-9da6-11ee-b164-01aa75ed71a1/language-en.

provisions so that Ketchie and manufacturers like us are able to continue the progress we made after 2017.

B. Congress Must Preserve Pro-Growth Tax Policies

As members of this committee are well aware, a number of other important tax policies enacted by the TCJA are set to expire at the end of 2025. These changes represent damaging tax increases for companies, like Ketchie, which will take effect if Congress does not act.

Ketchie is organized as an S corporation, and therefore is eligible for a 20% deduction on our business income thanks to the Section 199A provision created by the TCJA. Pass-through owners see their business income reflected on their personal tax returns, and this deduction reduces the amount of pass-through income subject to tax, allowing us to reinvest. This provision, along with the income tax rates for individuals, is set to expire at the end of 2025, dramatically increasing the tax burden on small manufacturers like Ketchie. This means we will have fewer resources to:

- Create new jobs;
- Create shadowing programs for our local high school;
- Invest in capital equipment;
- Improve our security systems and safety measures for our employees;
- Provide increased health benefits and 401(k) plans;
- Donate to local Boys & Girls Clubs;
- Increase bonus and pay scales for our employees; and
- Take chances on new innovations and technology to grow our business.

If Congress fails to preserve the 20% deduction, Ketchie will be unable to conduct these activities because funds will flow to the federal government instead of back to manufacturers so they can reinvest. I would like to thank Sen. Steve Daines for introducing the Main Street Tax Certainty Act, which would make the 20% deduction permanent for small manufacturers like Ketchie.

Moreover, if not for the federal estate tax exemption being increased in 2017, Ketchie might not be here today. I know firsthand the struggle that family-owned businesses face when a loved one passes away. When I lost my husband in 2014 to brain cancer, not only did I have to worry about keeping the business afloat, but I was so worried about a looming tax bill that might have forced us to halt production altogether.

We are a third-generation family-owned company, and we want to remain a lynchpin in Concord for many generations to come. The estate tax has a significant impact on family-owned manufacturers' ability to continue to operate after the death of a loved one. The tax has a disproportionate impact on family-owned manufacturers because their companies consist largely of illiquid assets that would need to be sold or leveraged to satisfy the tax burden.

In 2017, the TCJA increased the exemption threshold for the estate tax, allowing more of a family-owned business's assets to be passed on to the next generation without incurring a tax burden. The increased exemption is set to expire in 2026, which will expose more of a family-owned business's assets to taxation, making it increasingly difficult for them to continue operating and supporting local jobs following the death of a loved one. Preserving the TCJA estate tax or outright repeal would instill the confidence in small manufacturers like Ketchie that we will be able to continue operating in the event of losing a loved one.

Additionally, I encourage members of the committee to fully preserve stepped-up basis, which prevents a business owner's heirs from being forced to pay a capital gains tax on the asset appreciation that occurred during the owner's lifetime. A recent study found that taxing these unrealized gains would cost the U.S. economy 80,000 jobs per year over the course of a decade and 100,000 jobs per year thereafter.[9]

Manufacturers fully realize the task ahead for Congress is monumental. As they say though, the proof is in the pudding. The business tax policies implemented by the TCJA were rocket fuel for the manufacturing industry, and policymakers must act to ensure the U.S. manufacturing sector remains a global leader. Members of this committee must address the expired business tax provisions and reinstitute them as quickly as possible. Manufacturers appreciate the focus of this hearing today, and I hope that members of this committee and every member of Congress will institute tax policies that support manufacturers and provide tax certainty in 2025.

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I want to thank Chairman Wyden and Ranking Member Crapo for giving me the chance to testify today. Manufacturing truly is the backbone of our nation, and I appreciate all members of the committee continuing to give our industry the attention it deserves. Through sound tax policy, we will continue to create jobs, innovate, compete globally and provide a better future for young Americans.

Manufacturing truly is a team sport, and you are all on that team. Small companies like mine are counting on you to play with us rather than against us, and to ensure that our tax code does the same.

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[9] "Repealing step-up of basis on inherited assets: Macroeconomic impacts and effects on illustrative family businesses," EY (April 2021), *Available at* https://documents.nam.org/tax/ey-fbetc-stepupreport.pdf.