The Manufacturing Council

Appendix: Competitiveness Recommendations for Immediate Action

1. Institute comprehensive corporate tax reform. The corporate tax rate in the United States currently stands as the second highest among all major industrial nations and is a leading source of the significant financial disadvantage American manufacturers face in global markets. The taxation system has become exceedingly complex, requiring too much time, effort and money from manufacturers to ensure compliance while taking advantage of legal tax relief. The system of temporary renewals and frequent tax code changes creates uncertainty that often discourages investment and job creation. Reform should not only help reduce costs for American business, but should also provide clarity and long-term stability in corporate tax policies.

At a minimum, the Obama Administration should avoid measures that would create any additional tax burden for manufacturers, like the proposed elimination of the Last-In, First-Out (LIFO) accounting technique for inventory management, proposed in President's FY2012 budget, recently submitted to Congress. Administration estimates suggest that LIFO elimination would result in an additional tax liability of approximately $60 billion for U.S. business, hitting manufacturers particularly hard given high inventory levels common in the manufacturing sector.

As the Congress and the Obama Administration work toward comprehensive tax reform, there are three immediate action items that have the potential to make a dramatic contribution to manufacturing competitiveness:

ACTION: Reduce the U.S. corporate tax rate to 25 percent or lower without imposing offsetting tax increases.

> Manufacturers and other U.S. corporations play an integral role in our society and are major contributors to our country's economic growth and strong democratic government. Corporate America provides well-paying jobs for employees, investment opportunities for shareholders and high-quality products and services for consumers. American businesses today operate in a fiercely competitive global marketplace, and a pro-growth competitive, pro-manufacturing tax system is critical to their ability to compete.
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> One of the most important things policymakers can do to create a competitive U.S. tax climate is to reduce the corporate tax rate to 25 percent or lower today

without imposing offsetting tax increases. The United States now has the second highest statutory corporate tax rate among the major industrial (OECD) countries, trailing only Japan. Furthermore, other countries have been regularly lowering their tax rates to encourage economic growth.

As mentioned in the letter, an analysis last year by The Milken Institute, “Jobs for America,” concluded that reducing U.S. corporate income tax rates to the average of OECD countries (from the current 35 percent to 22 percent) would stimulate growth in the manufacturing sector. By 2019, real GDP would increase by 2.2 percent (or $376 billion) and 2.13 million jobs would be created.

We must recognize, too, that even a rate of 25 percent only brings us to parity with other major industrial nations. Real competitiveness in the longer term requires us to be more aggressive, targeting a corporate tax rate in the range of 15 percent to 20 percent, especially as other nations continue to reduce their own tax rates. Additionally, we must recognize that many small and mid-size manufacturing companies are organized as “Subchapter S” corporations that will not benefit from a lower corporate tax rate under the current tax code. We recommend that broader tax reforms should include a mechanism that allows these S corporations to be treated as a separate category for taxation purposes, but in the meantime we recommend a reduction in individual income tax rates so as to avoid inhibiting the growth of small and medium manufacturers.

ACTION: Move the United States from a worldwide to a territorial tax system to reduce the double tax burden imposed by the United States. At a minimum, a new system must exempt all active foreign earnings from taxation and avoid the imposition of a stealth tax on foreign earnings through expense allocations.

For more than 40 years, the federal tax system - a key factor in the ability of U.S. companies to compete in the world market place - has remained a constant. When the current international tax rules were first put in place, significantly fewer taxpayers and transactions were affected by them. However, times have changed since these rules were enacted. The United States is no longer the dominant global player that it was in the 1960s and 1970s. Foreign competition is fierce both in the United States and globally. Capital is far more mobile, generating "tax competition" among countries interested in attracting investment.

The ability of U.S. companies to compete effectively in the global marketplace is critical to our country's future economic growth. Investment abroad by U.S. companies generates U.S. exports and supports jobs in the United States. Companies with operations abroad employ an estimated 22 million people in the U.S. - more than 19 percent of the private workforce and 53 percent of all manufacturing employees. Many of these U.S. jobs support and depend on overseas operations, particularly jobs tied to product development and research initiatives. If U.S. companies cannot compete abroad, the U.S. economy will suffer from the loss of foreign markets and the loss of domestic jobs that support operations in those markets.

Despite the benefits to the U.S. economy of having American companies expand beyond our shores, U.S. tax laws still make it more difficult for U.S. multinationals to thrive and compete in the global marketplace. In particular, the United States has a worldwide system that taxes income regardless of where it is earned, resulting in "double taxation" when the same foreign income is taxed by both the United States and the country in which it is derived.

In contrast, many of our trading partners have a territorial system of taxation under which companies only are subject to the tax laws of the countries where the income is earned and not the tax laws of the country where the foreign parent corporation is domiciled. As a result, U.S. multinationals generally are subject to more tax on their global profits than are foreign-based multinationals- a significant disadvantage when U.S. companies are competing against non-U.S. multinationals and local firms for projects located in foreign jurisdictions.

The U.S. tax code does include some provisions designed to address this "double tax" problem. For example, the tax on the earnings of a U.S. corporation's foreign subsidiary typically is not imposed until those earnings actually are brought back to the United States and foreign tax credit rules provide credits for taxes paid to foreign jurisdictions. Unfortunately, even though these rules were designed to prevent double taxation and level the playing field between U.S. companies and their foreign competitors, both of these mechanisms have been limited to the point that widespread double taxation of U.S. companies is prevalent and deferral has been significantly limited. The proper focus is not on "deferral" but on ensuring that profits are taxed where earned and only where earned.

Consequently, we recommend strongly that policy makers look at totally replacing our worldwide system with a territorial tax system. Moreover, the system should be structured to enhance U.S. competitiveness, not to raise revenue. In addition, any territorial system should be designed to reduce the double tax burden imposed by the United States. At a minimum, a new system must exempt all active foreign earnings from taxation and avoid the imposition of a stealth tax on foreign earnings through expense allocations.

The goal of policy makers should be to move to a territorial system as described above. A territorial tax system that completely or almost completely exempts foreign dividends from taxation can create powerful incentives for U.S. companies to repatriate foreign earnings. For example, legislation enacted in 2004 - the American Jobs Creation Act (AJCA) - included a temporary "tax holiday" for foreign earnings brought back and reinvested in the United States. Companies using this one-time opportunity to reinvest foreign earnings in the United States paid an effective 5.25 percent tax rate and brought back some $300 billion to the United States.[1] Adoption of comprehensive tax reform and a territorial tax system designed to increase the competitiveness of U.S. companies and increase U.S. investment and employment are critical. Comprehensive reform, coupled with a concurrent transition rule similar to the AJCA for current foreign earnings, has great potential to further promote U.S. investment and employment from U.S. companies.

ACTION: Enhance and make the R&D tax credit permanent.

The federal R&D tax credit was originally enacted 30 years ago and has been extended 14 times, most recently in 2010. The current credit is set to expire at the end of 2011. Although there have been changes to the credit over the years, the most significant change was the addition, in 2007, of a new credit formula called the Alternative Simplified Credit (ASC). The original 12 percent ASC rate was increased to 14 percent in 2009, and President Obama has proposed increasing the rate to 17 percent and making the credit permanent. The broader business community is advocating for a permanent credit with a 20 percent ASC.

This is a critically important issue for U.S. manufacturers, who claim nearly 70 percent of all R&D credits and perform half of all R&D in the nation. Nearly 18,000 companies of all sizes use the R&D Credit and roughly 20 percent of all business research in the United States is performed by companies with fewer than 500 employees.[2] On average, 70 percent of R&D credit dollars are used for salaries of workers engaged in U.S.-based R&D.

Once a global leader with the best R&D tax incentive in the world in the mid-1980s, the U.S. R&D tax credit has fallen behind, now ranking 24th among 38 industrialized countries offering R&D tax incentives.[3] The global race for R&D investment dollars is fierce and highly competitive, as evidenced by the U.S. share of global R&D falling from 39 percent in 1999 to 33 percent in 2007, while China's share increased fourfold.[4] China's increase in R&D spending accounted for nearly one-third of the global increase in R&D between 2001 and 2006.[5] A strengthened, permanent R&D tax credit will help restore the United States as the best place to foster innovation and will assure companies that the credit will be available during the life of an R&D project, which for manufacturers typically spans 5 to 10 years.

It is also important to note that the credit is a jobs credit – 70 percent of R&D credit dollars are used for salaries of workers engaged in U.S.-based R&D. According to The Milken Institute, strengthening and making the credit

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[1] Melissa Redmiles, The One-Time Recieved Dividends Deduction, Internal Revenue Service, Statistics of Income Bulletin, Washington, DC, Spring 2008, http://www.irs.gov/pub/irs-soi/08codivdeductbul.pdf.
[2] National Science Board, 2010, "Science and Engineering Indicators 2010," Arlington, VA, National Science Foundation, NSB 10-01), January 15, 2010, p.4-4.
[3] OECD report, "Science, Technology and Industry 2009 Scoreboard," December 2009.
[4] Ibid.
[5] OECD report, "Ministerial Report on the OECD Innovation Strategy," May 2010, p.8.

permanent could boost GDP by more than $200 billion, generate 316,000 manufacturing jobs and raise total employment by 510,000 within 10 years.[6]

2. Enact regulatory reform and provide immediate relief from regulations that threaten serious damage to American manufacturing competitiveness.

Department of Commerce Participation in Regulatory Review

The Department of Commerce must speak for manufacturing when rules are being considered and should provide a strong, thoughtful voice within the inter-agency review of proposed regulations. **ACTION: We recommend that the Secretary ensure that the Department of Commerce can strongly support the President's Executive Order 13563 on Improving Regulation and Regulatory Review by establishing a formal, accountable mechanism for engaging other agencies and the manufacturing industry in the review process.**

High Priority Regulations for Manufacturers

Consistent with the President's direction to agencies to review existing and proposed rules to impose the least burden on society and to maximize net benefits, we wish to highlight the following recommendations for additional scrutiny of the Department of Commerce. These proposals are not consistent with the goal of increasing the competitiveness of manufacturing in the United States and, if adopted in their present form, will harm the economy and job creation. We commend the Administration for its efforts to reconsider some of these proposals, but urge that more is necessary to ensure a robust economy and a strong manufacturing base.

EPA Regulation of Greenhouse Gas Emissions

On January 2, 2011, the EPA began regulating greenhouse gas (GHG) emissions from stationary sources under the Clean Air Act. While only the largest facilities will be regulated at first, this action sets the stage for future regulation of much smaller sources. Manufacturers are also concerned that states are unprepared for the new permitting requirements, which will cause significant delays. This permitting gridlock will discourage manufacturers from building new facilities or expanding their current facilities, hurting competitiveness and discouraging job creation. Furthermore, additional facilities - including hospitals, agricultural establishments and even the smallest businesses - will be phased in to the onerous permitting requirements in the near future. **ACTION: The EPA's regulation should be withdrawn or modified to provide manufacturers with more flexibility and lower cost implementation of these requirements.**

EPA NAAQS for Ozone

[6] Jobs for America: Investments and policies for economic growth and competitiveness," The Milken Institute, January 2010.

The EPA in January 2010 issued a reconsideration of the National Ambient Air Quality Standards (NAAQS) for ground-level ozone. Despite continued improvement in the nation's air quality, the EPA has proposed to tighten the standard from the existing 75 parts per billion (ppb) to a range between 70 ppb and 60 ppb. Our overriding concern with the proposal is that the high compliance costs associated with the more stringent ozone standard will hinder manufacturers' ability to add jobs and hurt our global competitiveness. One study estimated 60 ppb would result in the loss of 7.3 million jobs by 2020 and add $1 trillion in new regulatory costs per year between 2020 and 2030. The agency has delayed finalizing the rule until July 2011 to allow for continued analysis of the epidemiological and clinical studies used to recommend the ozone standard. **ACTION: The EPA should withdraw its proposal to further lower the standard.**

EPA Boiler MACT

The EPA recently finalized a rule that would establish more stringent emissions standards on industrial and commercial boilers and process heaters (i.e. Boiler MACT). While the final rule included some changes that would make the new standards less onerous for manufacturers, the fundamental "pollutant-by-pollutant" approach to setting the emission limits remains unchanged. Many manufacturers are still concerned that the standards are unachievable by most real-world boilers. Facilities installing new boilers will have to comply with the new standards immediately, and existing boilers must be upgraded in three years. These new boilers and upgrades still come at a considerable cost to manufacturers, costing jobs and hindering economic growth. **ACTION: The EPA should stay the current requirements while it works to reconsider sections of the regulation and change its overall approach.**

OSHA Noise and Musculoskeletal Disorder Recordkeeping Proposals

OSHA recently rescinded its plans to enforce noise level standards in a dramatically different way for some noise levels by redefining what is deemed “feasible” for employers to reduce overall noise in the workplace and requiring implementation of these actions unless an employer can prove making such changes will put it out of business. The agency also recently temporarily withdrew a troubling proposed rule that would require employers who have recorded musculoskeletal disorders on their log to also check a box in an MSD column that would be added to the log. Both of OSHA’s proposals would have resulted in highly burdensome and costly changes for manufacturers, dramatically reducing competitiveness and even jeopardizing the ability of some businesses to remain solvent. While the proposed rules have been rescinded or withdrawn, we remain concerned by signals that the Administration might reintroduce the proposed rules in altered form. **ACTION: The OSHA should announce that it will not repropose these costly and unnecessary changes in enforcement and record keeping.**

OSHA On-Site Consultation

There has been a significant shift by OSHA from a more collaborative posture to a more adversarial approach toward business. Employers, particularly small businesses, should be able to consult with OSHA and receive its assistance to better understand and comply with existing workplace safety standards to enhance the safety of their workplaces without fear of citations and fines. Recently, OSHA proposed a rule that would modify how voluntary participation in OSHA's small business consultation and SHARP program would operate. As a result, businesses will be more reticent to reach out to OSHA for help and less likely to participate in this program. Instead of deterring participation in these effective programs, OSHA should focus on developing incentives and strategies that will encourage as many employers as possible to participate. **ACTION: The OSHA should withdraw this proposed rule.**

OSHA Injury and Illness Protection Program

OSHA is developing a new regulation that would mandate a standard for employers' safety and health programs, referred to as an Injury and Illness Prevention Program. We are concerned that this new proposal may not take into account the efforts by employers who already have effective safety and health programs in place or how this new mandate would disrupt safety programs that have achieved measurable successes. It appears this proposal may allow OSHA investigators to substitute their judgment of the employer's plan on how to achieve compliance and whether some "injury" in the workplace should have been addressed in some way, even if these conditions were regulated under a specific standard or did not amount to a "significant risk" as required under the OSH Act. **ACTION: The OSHA should announce that it will not propose a new standard for employers' safety and health programs.**

NLRB Posting Requirement

The National Labor Relations Board (NLRB) recently closed its comment period for a proposed rule which would require all employers to post a notice to employees outlining their rights to unionize. The proposed rule goes further by requiring employers who use electronic means of communicating with their employees to send an electronic version of the notice. This proposed rule demonstrates a shift in posture taken by the board in being more aggressive with rulings on cases overturning decades of precedent and now proposed rules, which we believe is beyond the scope of the board's authority. The National Labor Relations Act clearly indicates the board is an adjudicating body when there are complaints of labor violations and to conduct elections. Nowhere in the act does it grant the NLRB the authority to compel employers who are not in the midst of a union election or subject to a labor violation to do anything. **ACTION: The**

NLRB's proposed rule is outside their scope of authority and should be rescinded.

<u>DOT Hours of Service Rulemaking</u>

The Department of Transportation's (DOT) Federal Motor Carrier Safety Administration (FMCSA) has announced changes to the trucking hours of service rules first implemented in 2004. It has proposed to reduce well-established 11-hour driving and 14-hour on-duty times for truckers and to introduce new rest mandates. Over the past six years, driver and motor carrier safety performance has improved, and truck-involved fatalities and injuries have markedly declined. For manufacturers and those dependent on a healthy manufacturing economy, changes to the rule will affect significantly distribution patterns, supply chains, just-in-time delivery standards, trucking capacity, adding operational costs. The FMCSA previously estimated that reducing the driving time by one hour and eliminating the 34-hour restart provision would cost affected industries more than $2 billion. While the DOT is adhering to the terms of a 2009 court negotiated settlement reached with Public Citizen by reviewing and reconsidering the 2008 Final Rule on Hours of Service, the Department is not obligated to alter the rule. The Department's recent public commentary on poor truck driver health and longevity is drawing some concern because the scientific data to justify a change in the current rule is not strong. Approximately 80 percent of the nation's freight by value moves by truck. **ACTION: The Department of Transportation should withdraw its proposed rule or finalize a rule consistent with the current rules that are in place.**

<u>SEC Special Disclosures Section 1502 (Conflict Minerals)</u>

The Manufacturing Council supports the underlying goal of Sec. 1502 to address the atrocities occurring in the Democratic Republic of Congo (DRC) and adjoining countries. We encourage the SEC to implement Sec. 1502 in a manner consistent with the realities of global supply chains, acknowledging the limited control downstream users have on the refiners/smelters and mines. A successful outcome is one that achieves the goals of the statute without unduly burdening legitimate trade. The wrong path on this rulemaking could end up costing industries more than $11 billion to comply. **ACTION: The SEC should proceed cautiously and adopt a much less burdensome method for compliance with this requirement.**

3. Support Innovation and Research and Development (R&D) as a key component of U.S. manufacturing competitiveness by enacting a permanent, strengthened R&D credit, establishing regional innovation clusters, facilitating R&D collaboration between federal agencies and manufacturers, and enhancing opportunities available to small business through the Small Business Innovation Research (SBIR) grant program and the defense contracting process.

U.S. Government Investment in R& D

Innovation is central to American manufacturing jobs and competitiveness in the global economy. Investment in basic research is a critical component of America's innovation system.

Manufacturers conduct some basic research, but most of their investment is dedicated to applied R&D. Only the federal government has the resources to invest in long-term, high-risk/high-reward basic research that private companies cannot perform.

A number of U.S. federal government programs and initiatives must be continued and enhanced for the American manufacturing industry and the jobs it supports and creates to maintain its global leadership position. Manufacturers recommend the federal government do the following:

Fund the America COMPETES Act – Our economic future relies more than ever on our ability to innovate. The COMPETES Act will help manufacturers prosper in a globally integrated and highly competitive marketplace. The COMPETES Act reauthorizes critical programs ranging from federal funding for R&D to vital education grants, which will aid manufacturers and enhance their competitiveness.

Develop and Fund Regional Innovation Clusters – Regional Innovation Clusters (RICs) authorized in the COMPETES Act are designed to strengthen regional economies and advance the work in a given field by leveraging collaboration and communication between businesses and other entities. We recommend strengthening federal support for RICs by:

- Accelerating Economic Development Administration research to map clusters and development of related grant programs;
- Expanding federal resources available for targeted capital investment in RICs and streamlining the application/review process for funding; and
- Increasing direct federal agency participation in collaborative innovation projects underway in established RICs.

Continue the Manufacturing Extension Partnership Program (MEP) – The MEP is critical to the creation and retention of U.S. manufacturing jobs. Each year, the program is validated by an independent third party, which reported that the MEP program created and retained 72,075 jobs in FY09 alone and more than 318,000 since the program was created in 1988. In FY09, this public/private program created or retained $8.4 billion in sales, allowed its clients to make $1.9 billion in new investments and provided $1.3 billion in cost savings (based on 7,786 clients surveyed in FY10).

Continue the SBIR and Expand It to Benefit Medium-Size Manufacturers – The SBIR enhances opportunities available to small business, and could also become a resource for mid-size manufacturers. The risk and expense of conducting serious R&D efforts are often beyond the means of many small businesses, a challenge many medium-size businesses also face. By reserving a specific percentage of federal R&D funds for small and medium business, the SBIR reduces risk and enables them to compete on the same level as larger businesses. The SBIR funds the critical startup and development stages and encourages the commercialization of the technology, product, or service, which, in turn, stimulates the U.S. economy.

Provide Federal Government Loan Guarantees for Innovative Technology Research – The COMPETES legislation includes innovative technology federal loan guarantees for small- and medium-sized manufacturers – to expand, use innovative technology, or manufacture or commercialize an innovative technology product or process – to help them access capital to become more efficient and stay competitive.

Increas*e R&D Collaboration between Federal Agencies and Manufacturers –* The COMPETES Act will coordinate manufacturing R&D carried out across the federal government. It also authorizes the National Science Foundation (NSF) to support fundamental research leading to transformative advances in manufacturing. In addition, COMPETES establishes a clean energy manufacturing and construction initiative to create clean energy jobs, promote sustainability in manufacturing and bolster energy performance and air quality in buildings. Federal agencies should pay special attention to strengthening efforts to engage with university programs that have the potential to spark new innovation in the manufacturing sector.